United States Court of Appeals

for the Second Circuit

APPENDIX

74-2697

United States Court of Appeals

FOR THE SECOND CIRCUIT

B

P/S

AID AUTO STORES, INC.,

Plaintiff-Appellant,

—against—

HERBERT S. CANNON and CANNON, JEROLD & CO., INC.,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

APPENDIX

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Relevant Docket Entries

FILED	PROCEEDINGS
11–14–73	Filed Complaint issued summons.
11–16–73	Filed Notice of Removal.
12–10–73	Filed Stip & Order that the time for defts. Rittmaster Lawrence & Co., Inc., Arthur Rittmaster Jr., Lee Lawrence & Emanuel Iwanier to answer is extended to 12/20/73. Cooper J.
12 –6–73	Filed Summons and marshals ret. Served: Emanuel Iwanier on 11/19/73 Lee Lawrence on 11/19/73 Arthur Rittmaster Jr. on 11/19/73 Rittmaster, Lawrence & Co. Inc. on 11/19/73 Philips Appel & Walden Inc. on 11/20/73 Herbert S. Cannon on 11/20/73 Unable to Serve Cannon Jerold & Co. Inc.
1–17–74	Filed Third Party Complaint.
1–17–74	Filed Defts. Rittmaster Lawrence & Co., Inc., Arthur Rittmaster Jr., & Lee Lawrence ANSWER & Cross Claim.
1–25–74	Filed affdvt & order for service by an individual —Clerk.
2–15–74	Filed pltff's notice to take depositions of A. Rittmaster and H. S. Cannon.

Relevant Docket Entries

FILED	PROCEEDINGS
2–20–74	Filed stip & order extending 3rd pty deft's time to answer to 2-22-74—Cooper, J.
2–26–74	Filed 3rd pty defts. Herbert Eisenberg & Murray Klein ANSWER to 3rd pty complaint.
3– 7–74	Filed stip & order extending 3rd pty deft's (A. Biegen) time to answer to 4-12-74—Cooper, J.
3–12–74	File 3rd pty deft. Arnold L. Biegen ANSWER to 3rd pty complaint.
3–12–74	Filed 3rd defts. Notice of Appearance.
3–19–74	Filed ANSWER & Crossclaims of Defts. Herbert S. Cannon & Cannon Jerold & Co., Inc.
3–19–74	Filed ANSWER OF DFTS. HERBERT S. CANNON & CANNON JEROLD & CO. INC., TO CROSS CLAIM.
3–21–74	Filed Stip & Order that the time for deft's H. S. Cannon & Cannon Jerold & Co. to answer to cross claim of defts. Rittmaster Lawrence & Co., Inc., et al. is extended to 3/15/74. Cooper, J.
3–21–74	Filed Stip & Order that the time for defts. H. S. Cannon & Cannon Jerold & Co. to answer is extended to 3/15/74. Cooper, J.
3–27–74	Filed Summons (3rd pty) & marshals ret. Served: Arnold Biegen on 1/24/74

Relevant Docket Entries

FILED	PROCEEDINGS
	Mihon Wallace on 1/25/74
	Luis Neufeld on 1/22/74
	Martin Goldberg on 1/25/74
	Morris Clauman on 1/29/74
	Irving Poploff on 3/12/74
	Unable to Serve: Murray Klein, Herbert Eisenberg.
11–18–74	Filed pltffs' motion to strike jury demand.
11–18–74	Filed pltff's supplemental trial memorandum & in support of motion to strike.
11–20–74	Filed Memo. End. on motion dtd. 11/18/74. Motion denied. See Trial Minutes of this day. So Ordered Cooper, J. (mailed notice)
11–19–74	Before Cooper, J.—Jury Trial begun.
11–20–74	Trial Cont'd and Concluded—All claims settled between parties except Herbert S. Cannon & Cannon, Jerold & Co.—.
12– 4–74	Filed defts' (Cannon et ano) affdvt & notice of motion for costs—Ret. 12-13-74.
12– 3–74	Filed transcript of record of proceedings of Nov. 19, 20, 1974.
12–12–74	Filed stip of settlement—3rd pty complaint is withdrawn. Money judgment to be entered

Relevant Docket Entries

FILED	PROCEEDINGS
	against Arthur Rittmaster, Jr. & Lee Lawrence on consent. So ordered—Cooper, J.
12–13–74	Filed JUDGMENT—The complaint is hereby dismissed against defts. Herbert S. Cannon Cannon missed against defts. Herbert S. Cannon Cannon, Jerold & Co., Inc. & all other defts. appearing herein. The cross-claim of defts. Herbert S. Cannon and Cannon, Jerold & Co be dismissed as moot, and that the 3rd pty complaint be dismissed—Cooper, J. Judgment Entered—Clerk.
12–20–74	Filed pltff's notice of appeal from judgment entered 12-13-74. Mailed notice to Thal & Youtt.
1–28–75	Filed notice of certification & transmittal to the U.S.C.A. this date.
1–28–75	Filed Memorandum OPINION #41,814—In addition to costs to be awarded the deft., the judgment to be entered herein will provide for attys' fees in the amount of $8,480, the reasonableness of which is not contested, the pltff's contention being solely that the Court is without power in these circumstances to make any award for counsel fees. So Ordered—Cooper, J. Mailed notices.
1–28–75	Filed pltff's affdvt in opposition to motion for costs.

Complaint

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

73 Civ. 4890

AID AUTO STORES, INC.,

Plaintiff,

—against—

HERBERT S. CANNON, PHILIPS APPEL & WALDEN, INC., CANNON, JEROLD & CO., INC., RITTMASTER, LAWRENCE & CO., INC., ARTHUR RITTMASTER, JR., LEE LAWRENCE, EMANUEL IWANIER, MORI AARON SCHWEITZER and DAVID A. WOOLDRIDGE,

Defendants.

Plaintiff Aid Auto Stores, Inc. ("Aid" herein) for its complaint alleges:

Jurisdiction, Venue and Parties

1. This action arises under the Securities Act of 1933 ("1933 Act"), as amended (15 U.S.C. § 77a *et seq.*) and the Securities Exchange Act of 1934 ("1934 Act"), as amended (15 U.S.C. § 78a *et seq.*). The jurisdiction of this court is conferred by Section 22 of the 1933 Act (15 U.S.C. § 77v) and by Section 27 of the 1934 Act (15 U.S.C. § 78aa).

2. This action also arises under the corporation laws of the State of New York (N.Y. Business Corporation Law § 101 *et seq.*) and under the common law, respecting which this court has pendent jurisdiction.

3. Plaintiff Aid is and at all relevant times was a Delaware corporation with its principal place of business at 34-36 65th Street, Woodside, New York. Aid owns a chain of retail automotive supply stores located in New York and Florida, and grants franchises to other such stores. Aid is engaged in the wholesale distribution of automotive parts, supplies, tires, batteries and high performance items.

4. Upon information and belief, defendant Herbert S. Cannon ("Cannon" herein) carried out his business activities through and was until recently Chairman of the Board of defendant Cannon, Jerold & Co., Inc., ("Cannon Jerold" herein), 77 Water Street, New York, New York, an investment firm, and is now president of defendant Philips Appel & Walden, Inc. ("Philips Appel" herein), 111 Broadway, New York, New York, also an investment firm, which is the successor in interest to and is subject to the liabilities of Cannon Jerold. At all relevant times Cannon was a member of the Executive Committee of the Atlantic-Pacific Bank & Trust Company, Ltd., Nassau, Bahamas ("Bahamas Bank" herein), a bank chartered under the laws of the Bahamas and which is now in liquidation.

5. Upon information and belief, defendant Rittmaster, Lawrence & Co., Inc., ("RLC" herein) a corporation with a principal place of business at 363 Seventh Avenue, New York, New York, is an investment firm of which defendants Arthur Rittmaster, Jr. ("Rittmaster" herein) and Lee Lawrence ("Lawrence" herein) are principals. Defendant Emanuel Iwanier ("Iwanier" herein) is and at all relevant times was employed as Manager of RLC's Money Department.

6. From January 25, 1973 until October 1973 Rittmaster was an Aid director and from April 1973 until October 1973 was a member of the Executive and Finance Committees of Aid's Board of Directors.

7. Upon information and belief, defendant Mori Aaron Schweitzer ("Schweitzer" herein) a resident of the State of California, was at all relevant times President and Chairman of the Board of the Bahamas Bank.

8. Upon information and belief, defendant David A. Wooldridge ("Wooldridge" herein), a resident of Newport Beach, California, during a certain relevant period held a power of attorney from Schweitzer authorizing Wooldridge to perform the functions of President and/or Chairman of the Board of the Bahamas Bank.

9. Each defendant named herein transacts business or is otherwise found in the Southern District of New York and the offer and sale of the relevant security took place within this District, and the wrongful acts complained of took place primarily within this District.

First Claim
Against All Defendants
Sale of Unregistered Securities

10. On or about November 30, 1972 RLC acted as lead underwriter in a public offering of Aid common stock. RLC's underwriting compensation included, among other things, a two-year financial consulting agreement under which RLC has been paid by Aid $44,000, the total amount due, and the right to designate a director upon Aid's Board of Directors. On or about January 25, 1973 RLC desig-

nated Rittmaster who was then duly elected as an Aid director.

11. In or about March 1973 Rittmaster individually and as RLC's designee on Aid's Board of Directors recommended to Aid that a $400,000 certificate of deposit which Aid had purchased from a New York City bank be divided upon maturity into certificates of deposit purchased from several different banks in order to achieve a broader banking base. Rittmaster specifically recommended purchase of a $100,000 certificate of deposit from a New Jersey bank and of a certificate of deposit in an equal amount from the Bahamas Bank.

12. In or about April 1973, in reliance upon Rittmaster's recommendation, Aid purchased two $100,000 certificates of deposit from the New York bank and one $100,000 certificate of deposit from the New Jersey bank.

13. On April 3, 1973, also in reliance upon Rittmaster's recommendation, Aid mailed a check for $100,000 to the Bahamas Bank. On April 11, 1973 Murray Klein ("Klein" herein), Aid President, received a telephone call from Rittmaster advising that the Bahamas Bank had not received the check. Rittmaster stated that Schweizer would be in RLC's offices on April 13, 1973 and requested that Aid stop payment on its April 3rd check and issue a new check for personal delivery to Schweitzer on April 13th.

14. On April 12, 1973 by telephone and by letter Klein asked Rittmaster to furnish Aid as soon as possible with a copy of the Bahamas Bank's most recent financial statement.

15. On April 13, 1973 Klein, having stopped payment on the original check as requested by Rittmaster, had the second check personally picked up by a representative of RLC and delivered to Schweitzer at RLC's offices at 363 Seventh Avenue, New York, New York and Aid subsequently received a $100,000 certificate of deposit from the Bahamas Bank (the "C.D." herein) at 8½% interest to mature October 13, 1973, which C.D. was an unregistered security within the meaning of the 1933 and 1934 Acts. Aid's check was endorsed for the Bahamas Bank by Wooldridge.

16. On April 25, 1973 at a meeting of the Aid Board of Directors Rittmaster and Lawrence represented to the Board, among other things, that purchase of the Bahamas Bank's C.D. was a sound investment because it would interest foreign investors in Aid's stock. In reliance on that representation the Board then ratified the purchase of the C.D. Several Board members did express reservations about the Bahamas Bank as a result of which Klein, by numerous telephone calls and by letter of April 30, 1973 repeatedly and again requested Rittmaster to furnish Aid with a copy of the Bahamas Bank's financial statement.

17. On May 24, 1973, at the Aid annual shareholders meeting, Rittmaster delivered to Klein a combined financial statement for the Bahamas Bank and another Nassau bank which showed that as of November 1, 1972 well over half of the combined claimed assets of $3,600,000 consisted of deposits of a predecessor bank which could not be transferred to the successor without written depositor approval. After review of this financial state-

ment Klein, by letter of May 24, 1973, requested Rittmaster to arrange for immediate retirement of the C.D. since it was impossible to determine the Bahamas Bank's net worth from the financial statement.

18. Between May 24, 1973 and July 18, 1973 Klein made several telephone and letter requests to Rittmaster and Schweitzer and Bahamas Bank for immediate retirement of the C.D., all of which went unheeded.

19. On August 7, 1973 Klein was informed by the Bahamas Bank that the C.D. could be called for early maturity only upon forfeiture of all accrued interest and payment of a one percent of principal penalty. Klein was aso informed that in consideration of placement of the C.D. the Bahamas Bank had made a $50,000 unsecured loan to RLC and paid a $1,500 fee to RLC. Klein requested immediate retirement of the C.D. on the terms specified.

20. During the last week of August, 1973 Klein was informed by the Bahamas Bank that Wooldridge had ordered that the C.D. not be retired because RLC had not repaid its loan. Klein's repeated requests to Schweitzer and the Bahamas Bank for immediate retirement were unsuccessful.

21. In September, 1973 Aid was informed by Bahamas counsel that the Bahamas Bank's license had been revoked by the Bahamas banking authorities and that the Bahamas Bank appeared to have no liquid assets.

22. On October 3, 1973 Rittmaster stated to Aid that he had first become involved with the Bahamas Bank through

Cannon; that Cannon was associated with the Bahamas Bank which was known as "Cannon's bank"; that Cannon had arranged with him for the payment of fees in return for placing certificates of deposit of the Bahamas Bank; that he and Lawrence had each received a personal loan of $25,000 from the Bahamas Bank in return for selling the C.D. to Aid; that Iwanier of RLC had received a $1,500 commission from Bahamas Bank for placement of the C.D.

23. Prior to Aid's purchase of the C.D. and continuing thereafter, and unknown to Aid, defendants Cannon, Cannon Jerold, Philips Appel, Schweitzer, Wooldridge and others on behalf of the Bahamas Bank had agreed to pay commissions and fees to RLC, Rittmaster, Lawrence, Iwanier and others for the sale of certificates of deposit of the Bahamas Bank to third parties. In at least one instance, on or about February 28, 1973, Cannon and Cannon Jerold personally guaranteed payment of such commissions to RLC.

24. During the first four months of 1973 and at other times all defendants, in violation of Section 5 of the 1933 Act (15 U.S.C. § 77e) and through the use of interstate telephone calls, the mails and interstate transportation, instrumentalities of interstate commerce, did both offer to sell and sell certificates of deposit of the Bahamas Bank, including the C.D., without compliance with the registration requirements of the 1933 Act.

25. By reason thereof plaintiff has suffered damages in the amount of $147,000.

Complaint

Second Claim
Against All Defendants
Misleading Offer to Sell Securities

26. Plaintiff repeats and realleges each and every allegation contained in paragraphs 1 through 23 as though fully set forth herein.

27. All defendants, during the first four months of 1973, by the use of interstate telephone calls, the mails and interstate transportation, instrumentalities of interstate commerce, offered to sell and sold certificates of deposit of the Bahamas Bank, including the C.D., by means of oral communications which omitted to state a material fact necessary to make the statements, in light of the circumstances under which they were made, not misleading, i.e. that the Bahamas Bank was virtually insolvent, in violation of Section 12(2) of the 1933 Act (15 U.S.C. § 77l(2)).

28. By reason thereof, plaintiff has suffered damages in the amount of $147,000.

Third Claim
Against All Defendants
Use of Manipulative and Deceptive Devices

29. Plaintiff repeats and realleges each and every allegation contained in paragraphs 1 through 23 as though fully set forth herein.

30. All defendants, with full knowledge of the precarious financial condition of the Bahamas Bank, and by the use of interstate telephone calls, the mails and interstate transportation, instrumentalities of interstate commerce, have

employed a device, scheme or artifice to defraud plaintiff and others into purchasing certificates of deposit of the Bahamas Bank, have made untrue statement of material facts and have omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, and have engaged in acts, practices or courses of business which operated as a fraud or deceit upon plaintiff in connection with the purchase or sale of the C.D. in violation of Section 10(b) of the 1934 Act (15 U.S.C. § 78j(b)) and Rule 10b-5 promulgated thereunder.

31. By reason thereof plaintiff has suffered damages in the amount of $100,000.

Fourth Claim
Against All Defendants
Common Law Fraud

32. Plaintiff repeats and realleges each and every allegation contained in paragraphs 1 through 23 as though fully set forth herein.

33. All defendants joined in a common scheme and conspiracy, to make knowingly false representations, which each and every defendant knew to be false at the time they were made and which each and every defendant intended plaintiff to rely upon, to plaintiff and others concerning the Bahamas Bank as an appropriate investment. Said scheme and conspiracy including omitting to tell plaintiff that the Bahamas Bank was virtually insolvent. Plaintiff was wholly deceived by this fraudulent scheme and conspiracy and relied upon these false representations in purchasing the C.D.

34. By reason thereof plaintiff has suffered damages in the amount of $147,000.

Fifth Claim
Against Defendants Rittmaster,
Lawrence, Iwanier and RLC
Breach of Director's Duties

35. Plaintiff repeats and realleges each and every allegation contained in paragraphs 1 through 23, as though fully set forth herein.

36. By recommending the Bahamas Bank as an appropriate investment for plaintiff and by accepting a personal loan and a commission paid to RLC in return for sale of the C.D. to plaintiff, Rittmaster, in violation of N. Y. Business Corporation Law § 717, breached his duty as an Aid director to exercise good faith and has usurped a corporate opportunity for his own benefit and purposes in violation of his fiduciary duty of loyalty and allegiance to plaintiff.

37. By reason thereof plaintiff has suffered damages in the amount of $147,000.

Sixth Claim
Against RLC
Breach of Contract

38. Plaintiff repeats and realleges each and every allegation contained in paragraphs 1 through 23, as though fully set forth herein.

39. RLC by its bad faith recommendation to purchase the C.D. and by accepting a commission in return for sale

of the C.D. has breached its express contractual duty to in good faith advise and assist plaintiff concerning financing.

40. By reason thereof plaintiff has suffered damages in the amount of $147,000.

Seventh Claim
Against Cannon, Cannon Jerold
and Philips Appel

41. Plaintiff repeats and realleges each and every allegation contained in paragraphs 1 through 23 as though fully set forth herein.

42. Defendants Cannon and Cannon Jerold procured and induced the disloyalty and violation of fiduciary obligation and breach of contract on the part of RLC, Rittmaster, Lawrence and Iwanier, and caused, induced and procured the violations of law hereinbefore alleged, and defendant Philips Appel also procured and induced such wrongful acts and violations or by reason of becoming the successor in interest to and being subject to the liabilities of Cannon Jerold, is also responsible for such wrongful acts and violations of law.

43. By reason therefor plaintiff has suffered damages in the amount of $147,000.

WHEREFORE, plaintiff demands judgment against the defendants, and each of them, jointly and severally:

On the first claim for $147,000;

On the second claim for $147,000;

On the third claim for $100,000;

On the fourth claim for $147,000;

On the fifth claim for $147,000;

On the sixth claim for $147,000; and

On the seventh claim for $147,000

together with interest thereon and the costs and disbursements of this action, together with reasonable attorneys fees.

Dated: New York, New York
November 13, 1973

ROGERS HOGE & HILLS

/s/ Clendon H. Lee

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Answer and Cross-Claims of Defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

DEFENDANTS CANNON and CANNON JEROLD DEMAND TRIAL BY JURY

Defendants, Herbert S. Cannon and Cannon, Jerold & Co., by their attorneys Thal & Youtt, for their answer to the complaint herein, state as follows:

1. Deny the allegations contained in Paragraphs "1" and "2" of the complaint insofar as those allegations relate to the defendants above named.

2. State that they are without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph "3" of the complaint.

3. Deny that the address of defendant Cannon, Jerold & Co., Inc. ("Cannon Jerold") is 77 Water Street, New York, New York and that defendant Cannon is its Chairman of the Board, admit that defendant Cannon is president of another named defendant, Philips Appel & Walden, Inc., ("Philips Appel"), as alleged in Paragraph "4" of the complaint, but deny that defendant Philips Appel is the "Successor in interest to and is subject to the liabilities of" defendant Cannon Jerold and deny that defendant Cannon "carried out his business activities through" defendant Cannon Jerold.

Answer and Cross-Claims of Defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

4. Further answering Paragraph "4" of the complaint, defendants admit that at all relevant times, the Atlantic-Pacific Bank & Trust Company, Ltd., Nassau, Bahamas ("Bahamas Bank") was chartered under the laws of the Bahamas and that the said bank is now in liquidation but deny that at all relevant times, defendant Cannon was a member of the Executive Committee of the Bahamas Bank.

5. State that they are without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraphs "5" through "8" of the complaint.

6. State that they are without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph "9" of the complaint except admit that defendants Cannon and Cannon Jerold either transact business or are "otherwise found" in the Southern District of New York.

As to the First Claim of the Complaint

7. State that they are without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraphs "10" through "14".

8. State that they are without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraph "15" of the complaint.

9. State that they are without knowledge or information sufficient to form a belief as to the truth of the allegations contained in Paragraphs "16" through "22".

Answer and Cross-Claims of Defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

10. Deny the allegations contained in Paragraphs "23" through "25" of the complaint, insofar as said allegations refer or relate to defendants Cannon and/or Cannon Jerold.

As to the Second Claim of the Complaint

11. With respect to the allegations contained in Paragraph "26" of the complaint, defendants repeat and reallege each and every denial, denial of knowledge or information, and admission made with respect to the allegations contained in Paragraphs "1" through "23" of the complaint as though the same were set forth again at length herein.

12. Deny the allegations contained in Paragraphs "27" and "28" of the complaint, insofar as said allegations refer or relate to defendants Cannon and/or Cannon Jerold.

As to the Third Claim of the Complaint

13. With respect to the allegations contained in Paragraph "29" of the complaint, defendants repeat and reallege each and every denial, denial of knowledge or information, and admission made with respect to the allegations contained in Paragraphs "1" through "23" of the complaint as though the same were set forth again at length herein.

14. Deny the allegations contained in Paragraphs "30" and "31" of the complaint insofar as said allegations refer or relate to defendants Cannon and/or Cannon Jerold.

Answer and Cross-Claims of Defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

15. With respect to the allegations contained in Paragraph "32" of the complaint, defendants repeat and reallege each and every denial, denial of knowledge or information, and admission made with respect to the allegations contained in Paragraphs "1" through "23" of the complaint as though the same were set forth again at length herein.

16. Deny the allegations contained in Paragraphs "33" and "34" of the complaint insofar as said allegations refer or relate to defendants Cannon and/or Cannon Jerold.

As to the Fifth and Sixth Claims of the Complaint

17. Defendants Cannon and Cannon Jerold make no response to the Fifth and Sixth Claims of the Complaint (Paragraphs "35" through "40") as those claims are not directed against them.

As to the Seventh Claim of the Complaint

18. With respect to the allegations contained in Paragraph "41" of the complaint, defendants repeat and reallege each and every denial, denial of knowledge or information, and admission made with respect to the allegations contained in Paragraphs "1" through "23" of the complaint as though the same were set forth again at length herein.

19. Deny the allegations contained in Paragraphs "42" and "43" of the complaint insofar as said allegations refer or relate to defendants Cannon and/or Cannon Jerold.

Answer and Cross-Claims of Defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

First Affirmative Defense

20. The Complaint fails to state a cause of action against defendants Cannon and Cannon Jerold.

Second Affirmative Defense

21. On information and belief the certificate of deposit complained of in the Complaint (the "C.D.") was one of an insubstantial number of certificates of deposit offered for sale by the Bank in the United States. Certificates of deposit were not offered to the public generally, but were reserved to a limited number of offerees. Sale of the C.D. was affected by direct negotiation between plaintiff and the Bahamas Bank, and it was at all times contemplated by the Bank that sales of other certificates of deposit to United States investors would be effected in the same fashion.

22. Any offer of certificates for sale in the United States was limited to persons capable of making informed investment decisions, which persons would be capable of obtaining and analyzing the same kind of information that registration under the Securities Act would provide.

23. At all relevant times, plaintiff, with the assistance, advice, and counsel of its officers, directors, and agents, was capable of making such informed investment decisions and was capable of obtaining and analyzing the same kind of information that registration under the Securities Act would provide.

24. In effecting the purchase of the C.D., defendant Rittmaster, in his capacity as a director of plaintiff, was

acting as agent for plaintiff. In such capacity he, as well as persons acting under his direction and control, engaged in direct contact and negotiation with the Bahamas Bank, which negotiations culminated in the sale by the Bank to plaintiff of the C.D.

25. In such capacity, defendant Rittmaster and persons acting under his direction and control had an actual opportunity to inspect the Bahamas Bank's records and to verify any and all purchase-inducement representations made by the Bank.

26. By reason of the foregoing, the sale of a certificate of deposit as alleged in the Complaint, or certificates of the same class constituted a private offering in that it did not constitute a public offering within the meaning of Section 4(2) of the Securities Act of 1933 as amended (15 U.S.C. §77d(2)). Accordingly, defendants are not subject to the provisions of Section 5 of the Securities Act (15 U.S.C. §77e) and plaintiff is not entitled to the relief which it seeks against defendants Cannon and Cannon Jerold in the First Claim of the Complaint.

Third Affirmative Defense

27. On information and belief, the Bahamas Bank was not "virtually insolvent" during the first four months of 1973, contrary to the allegations contained in Paragraph 27 of the Complaint, as a consequence thereof, plaintiff was not misled by the failure or omission of any defendant or defendants to state that the Bank was virtually insolvent. Accordingly, plaintiff is not entitled to the relief which it seeks against defendants Cannon and Cannon

Jerold in its Second, Third, and Fourth Claims of the Complaint.

Fourth Affirmative Defense

28. Defendants Cannon and Cannon Jerold took no part in either the solicitation of plaintiff's offer to purchase the C.D., or in the actual sale of the C.D. itself. Indeed they did not learn of plaintiff's interest in purchasing the C.D. and of its actual purchase until after the date of sale. Further said defendants did not receive any commission, fees or other direct benefits as a consequence of the sale of the C.D.

29. As a consequence thereof, defendants Cannon and Cannon Jerold are not "persons who sold" within the meaning of Section 12 of the Securities Act as amended (15 U.S.C. §77 1) and accordingly, plaintiff is not entitled to the relief which it seeks against them in the First and Second Claims of the Complaint.

Fifth Affirmative Defense

30. In the alternative, if it be determined that defendants Cannon and/or Cannon Jerold are "persons" who could be subject to liability under §12 (2) of the Securities Act as amended (15 U.S.C. §771 (2)), they did not know, nor in the exercise of reasonable care could they have known that the Bahamas Bank was "virtually insolvent" or that the facts necessary to determine the true financial condition and stability of the Bank had been omitted in connection with the sale of the C.D. to plaintiff. Accordingly, pursuant to §12 (2) of the Securities Act as amended

(15 U.S.C. §771 (2)), plaintiff is not entitled to the relief which it seeks against said defendants in the Second Claim of the Complaint.

Sixth Affirmative Defense

31. At no time relevant hereto did defendant Cannon and/or defendant Cannon Jerold in any way possess the power to direct or cause the direction of the management and policies of the Bahamas Bank, either through ownership of voting securities, by contract, or otherwise. Accordingly, these defendants were not controlling persons of the Bahamas Bank within the meaning of §15 of the Securities Act as amended (15 U.S.C. §77 o), and plaintiff is not entitled to recover against them on the First and Second Claims of the Complaint.

Seventh Affirmative Defense

32. In the alternative to the allegations set forth in Paragraphs 27 and 31 above, if it be determined that defendants Cannon and/or Cannon Jerold were controlling persons within the meaning of §15 of the Securities Act as amended, (15 U.S.C. §77 o) and if it be determined that the Bahamas Bank was in fact "virtually insolvent" during the first four months of 1973 as alleged in Paragraph 27 of the Complaint, defendants Cannon and/or Cannon Jerold had no knowledge of nor reasonable ground to believe that the Bank was "virtually insolvent" nor that plaintiff had been prevented by the Bank or was otherwise unable to obtain all facts necessary to determine for itself the true financial condition and stability of the Bank at the time it purchased the C.D.

33. As a consequence thereof, by reason of the express terms of §15 of the Securities Act as amended, (15 U.S.C. §77 o), as well as general principles of common law, defendants Cannon and Cannon Jerold are not liable to plaintiff on the Second, Third, and Fourth Claims of the Complaint.

Eighth Affirmative Defense

34. Defendants Cannon and Cannon Jerold repeat and reallege the allegations contained in Paragraphs 23 through 25 above, as if fully set forth herein.

35. Prior to and at the time it purchased the C.D., plaintiff, through its agents, directors, and employees knew, or in the exercise of reasonable care, could have known of the Bahamas Bank's financial position and stability, including, if such is proven to be the case, its "virtual insolvency". Indeed, by virtue of its direct contacts with the Bahamas Bank, plaintiff was in at least as good a position as defendants Cannon and Cannon Jerold to obtain necessary and relevant audits, documents and other information and, on information and belief, at all times material hereto, said audits, documents and or other information were readily accessible to plaintiff.

36. As a consequence thereof, plaintiff is not entitled to recover against defendants Cannon and/or Cannon Jerold on the First and Second Claims of the Complaint.

Ninth Affirmative Defense

37. On information and belief, the C.D. which is the subject of this action was issued for purposes of obtain-

ing working capital for the Bahamas Bank, and the proceeds of its sale were so used. The C.D. was negotiable and discountable when issued and entitled the holder to receive the face amount plus stated interest at maturity, six months after date of issue.

38. The C.D. which is the subject of this lawsuit constitutes a banker's acceptance which arose out of a current transaction or the proceeds of which were to be used for current transactions, the maturity of which at time of issuance did not exceed nine months, exclusive of days of grace, within the meaning of Section 3(a)(3) of the Securities Act as amended (15 U.S.C. §77c (a) (3)).

39. As a consequence thereof, the C.D. constitutes an exempted security within the meaning of the Securities Act as amended and is not subject to the provisions of Section 5 of the Securities Act as amended (15 U.S.C. §77e) and plaintiff is not entitled to the relief which it seeks against defendants Cannon and Cannon Jerold in the First Claim of the Complaint.

Tenth Affirmative Defense

40. Defendants Cannon and Cannon Jerold repeat and reallege the allegations contained in Paragraphs "27", "30" and "32" above, as if fully set forth herein.

41. At all relevant times, prior to the sale of the C.D. to plaintiff and thereafter, defendant Cannon used his diligent efforts to determine that all information which he possessed and/or communicated with respect to the

Bahamas Bank was the complete truth and that no further information was necessary to make it complete.

42. In the event it is determined that untrue statements or omissions of material facts were made in connection with the sale of the C.D. to plaintiff, as alleged in Paragraph "30" of the Complaint, such statements or omissions were caused solely by the withholding of information by either the Bahamas Bank or defendants Schweitzer, Wooldridge, Rittmaster, Iwanier or Lawrence, or some combination of the above named defendants from defendant Cannon, as well as others, including plaintiff.

43. Accordingly plaintiff is not entitled to the relief which it seeks against defendants Cannon and Cannon Jerold on the Third Claim of the Complaint.

Eleventh Affirmative Defense

44. Defendants Cannon and Cannon Jerold repeat and reallege the allegations contained in Paragraphs "23"-"25" above, as if fully set forth herein.

45. On information and belief, plaintiff, prior to acquiring the C.D. which is the subject of this action, undertook, through one or more of its directors, officers, agents and/or representatives, to make a full investigation of the status and operations of the Bahamas Bank. Such investigation included one or more visits to the offices of the Bank in the Bahamas. Plaintiff's acquisition of the C.D. was made solely in reliance on said investigation and was in no way based on information supplied or not

supplied by either defendant Cannon or defendant Cannon Jerold. Defendants Cannon and/or Cannon Jerold took no part in the aforesaid investigation.

46. Further, on information and belief, plaintiff's investigation gave plaintiff the opportunity to obtain all of the facts regarding the status and operations of the Bahamas Bank, and plaintiff had full knowledge of all facts necessary to evaluate for itself the financial condition and general status of the Bank and hence, the advisability of acquiring the C.D. which is the subject of this litigation. Accordingly, plaintiff is not entitled to the relief which it seeks against defendants Cannon and Cannon Jerold on the Third Claim of the Complaint.

Twelfth Affirmative Defense

47. At all times from and after the time plaintiff acquired reason to question or suspect the financial condition or stability of the Bahamas Bank in the spring of 1973 or information which would have caused plaintiff not to purchase the C.D. had such information been available prior to purchase, plaintiff incurred the duty to mitigate or prevent loss to it by promptly retiring the C.D.

48. On information and belief, in or about June, July and August, 1973, plaintiff could have retired the C.D. upon forfeiture of accrued interest as well as a fee of $1,000 and upon arranging for the repayment by defendant Rittmaster, a director of plaintiff of a private loan extended by the Bahamas Bank to defendant Rittmaster or to his company, defendant Rittmaster Lawrence & Co., Inc. By so doing, plaintiff could have redeemed a substantial portion of the funds expended for the C.D. prior

to the time the Bahamas Bank was seized by government officials and its assets frozen, and thereby have mitigated the substantial losses which it now claims to have suffered.

49. By reason of the foregoing, if it be determined that the plaintiff is entitled to recover on the basis of any of the claims set forth in the Complaint, its recovery is limited to the sum which it would have lost had it retired the C.D. in June, July, or August of 1973.

Thirteenth Affirmative Defense on Behalf of Defendant Cannon Jerold

50. With respect to all of the circumstances, events, and transactions alleged in the complaint, in the event it is determined that defendant Cannon engaged in any conduct, made any statements, or omitted to make statements in connection with the sale of the C.D. to plaintiff, such conduct, statements, or omissions constituted private activity on his part alone and not for the benefit or on behalf of defendant Cannon Jerold. He was not specifically or generally authorized to act on behalf of defendant Cannon Jerold in such respects nor did he purport to do so.

51. Accordingly, defendant Cannon Jerold is not liable to plaintiff or to any other defendant by reason of any act or omission of defendant Cannon.

Cross-Claim Against Defendants Mori Aaron Schweitzer, David A. Wooldridge, Arthur Rittmaster, Jr., Lee Lawrence, and Emanuel Iwanier

52. Defendants Cannon and Cannon Jerold repeat and reallege the allegations contained in Paragraphs "23",

"24", "25", "42", and "45" above, as if fully set forth herein.

53. By reason of the matters alleged herein, if it be determined that plaintiff is entitled to recover on any of the claims alleged in the complaint, plaintiff's loss or damage has been caused solely by the negligent or intentional misrepresentations, misstatements, defaults, and/or failures of defendants Schweitzer, Wooldridge, Rittmaster, Lawrence, or Iwanier, or some or all of them, to disclose relevant and material information to plaintiff in connection with the sale of the C.D. which is the subject of this action.

54. In the event plaintiff recovers judgment against defendant Cannon and/or defendant Cannon Jerold then said defendants Cannon and Cannon Jerold are entitled to indemnification and judgment over in like amount against defendants Schweitzer, Wooldridge, Rittmaster, Lawrence and/or Iwanier.

WHEREFORE, defendants Cannon and Cannon Jerold demand judgment dismissing the complaint herein as it applies to them or alternatively, if judgment in favor of plaintiff against said defendants is rendered, that judgment over in the same amount of plaintiff's judgment be rendered in favor of defendants Cannon and Cannon Jerold against defendants Mori Aaron Schweitzer, David A. Wooldridge, Arthur Rittmaster, Jr., Lee Lawrence,

and Emanuel Iwanier, together with the costs, disbursements, and reasonable attorney's fees of this action.

THAL & YOUTT

By .....
A Member of the Firm
Attorneys for Defendants
Herbert S. Cannon and Cannon
Jerold & Co., Inc.
666 Fifth Avenue
New York, New York 10019
212, 586-3722

Motion for Costs

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

73 Civil 4890

[SAME TITLE]

PLEASE TAKE NOTICE:

Upon the annexed Affidavit of STEVEN H. THAL, the annexed Memorandum of Law and upon all of the pleadings and proceedings heretofore had in this matter, defendants Herbert Cannon and Cannon, Jerold & Co. will apply to this Court on December 13, 1974 at 10:00 o'clock in the forenoon, or as soon thereafter as counsel can be heard, before the Hon. Irving Ben Cooper, U.S.D.J. in Courtroom 110 at the United States Courthouse, Foley Square, New York, New York for an order requiring plaintiff to reimburse said defendants for costs incurred in connection with the defense of this action and for such other and further relief as to this Court may seem just and proper.

Dated: New York, New York
December 2, 1974

Yours, etc.

THAL & YOUTT
Attorneys for Defendants
Herbert S. Cannon and Cannon,
Jerold & Co.
666 Fifth Avenue
New York, New York 10019
212, 586-3722

To:

ROGERS HOGE & HILLS
Attorneys for Plaintiff
90 Park Avenue
New York, New York 10016
212, 953-9200

Affidavit of Steven H. Thal in Support of Motion for Costs

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

73 Civil 4890

[SAME TITLE]

STATE OF NEW YORK,
COUNTY OF NEW YORK, *ss.:*

STEVEN H. THAL, being duly sworn, deposes and says:

1. I am a partner in the law firm of Thal & Youtt, attorneys for defendants Herbert S. Cannon ("Cannon") and Cannon, Jerold & Co. ("CJC"). I am a duly licensed attorney in the State of New York, and I am admitted to practice before the United States District Court for the Southern District of New York.

2. The complaint in this action alleged that defendants Cannon and CJC had violated the Securities Laws of the United States and had committed various tortious acts under Common Law.

3. The issues were tried in this Court on November 19 and 20, 1974; and at the close of plaintiff's case, the defendants' motion for dismissal was granted.

4. By reason of the foregoing, defendants ask this Court to order that plaintiff's reimburse defendants for costs of depositions in the amount of $480.

Affidavit of Steven H. Thal in Support of Motion for Costs

5. In addition, defendants have expended large sums on attorneys' fees in preparing their defense. Defendants request that this Court order that plaintiff reimburse them for said fees which are in the nature of costs under the Securities Laws of the United States.

6. Section 11(e) of the Securities Act of 1933, as amended, provides in relevant part:

> In any suit *under this or any other section of this title* the court may, in its discretion, require an undertaking for the payment of the costs of such suit, *including reasonable attorney's fees,* and if judgment shall be rendered against a party litigant, upon the motion of the other party litigant, such costs may be assessed in favor of such party litigant (whether or not such undertaking has been required) *if the court believes the suit or the defense to have been without merit, in an amount sufficient to reimburse him for the reasonable expenses incurred by him,* in connection with such suit, such costs to be taxed in the manner usually provided for taxing of costs in the court in which the suit was heard (emphasis added). 15 USC 77K(e).

The instant case is a most appropriate situation in which attorney's fees should be included in costs.

7. The plaintiff brought this suit in federal court by alleging Securities Law violations and also including Common Law violations under the doctrine of pendant jurisdiction.

Affidavit of Steven H. Thal in Support of Motion for Costs

At trial plaintiff based its case entirely on the concept of "commercial bribery" which was alleged in the Seventh Claim of the Complaint and based on Common Law. Further, plaintiff's trial memorandum and proposed jury instructions focused almost exclusively on the issues raised in the Seventh Claim.

Therefore, plaintiff did not even attempt to make a prima facie case under the Securities Laws and it appears that such allegations were made solely for the purpose of obtaining federal court jurisdiction by pleading a federal statute.

Without the Securities Law allegations there would have been no jurisdiction in the Federal Court since there was no complete diversity. Plaintiff has its principal place of business in New York and certain defendants have their principal places of business in New York (e.g. Cannon, Jerold & Co., Philips, Appel & Walden, Inc.).

8. At the close of plaintiff's case, the Court, on motion, dismissed plaintiff's case by reason of the fact that proof of each allegation was so weak that reasonable minds could not conclude that there was any violation of either Securities Laws or Common Law.

9. In addition to these legal points, defendant Cannon made every effort to mitigate his legal fees in this matter by attempting in good faith to settle the claim before trial. Without admitting any liability, Cannon offered $10,000 to plaintiff many months before trial. This offer was renewed a few weeks before trial. In response, plaintiff's counsel wrote to the Court that plaintiff had received only

a "nominal" offer (See Exhibit A attached hereto). When the Court instructed counsel to make one last settlement effort on the eve of trial, I contacted Mr. Cannon to discuss an increase of the settlement offer and advised him that he could add the attorneys' fees for trial into his prior offer. Although Mr. Cannon could not raise more cash at this time due to liquidity problems, we arranged a list of securities which we could offer together with some cash in order to increase the offer. I called plaintiff's counsel on Sunday night with such an offer and he refused to even negotiate at less than $75,000, and further stated that such amount had to be secured by a mortgage on Mr. Cannon's house. The failure of this effort was reported by me to the Court on the day before trial.

10. In the preparation of this case my law firm spent in excess of 120 hours. Due to the seriousness of the allegations under the Securities Act and the charge of commercial bribery; we undertook extensive investigations concerning the Bahamas Bank, made contact with representatives of the Bahamas Government and prepared substantial legal documents.

11. While much of this effort never appeared at trial due to the weakness of plaintiff's case, we were prepared to present a total defense to each and every charge in the complaint.

12. Given these facts and the total failure of plaintiff to make out any case under the Securities Laws or any other law, I believe this litigation was "without merit"

Affidavit of Steven H. Thal in Support of Motion for Costs

and should never have been heard in Federal Court and therefore defendants should be entitled to recover attorneys fees in the amount of $8,000 plus $480 for deposition costs.

/s/ Steven H. Thal

(Sworn to November 27, 1974.)

Affidavit in Opposition to Motion for Costs

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

73 Civil 4890 (IBC)

[SAME TITLE]

STATE OF NEW YORK,
COUNTY OF NEW YORK, *ss.*:

CLENDON H. LEE, being duly sworn, deposes and says:

1. I am a member of Rogers Hoge & Hills, attorneys for plaintiff Aid Auto Stores, Inc. and am familiar with the facts hereinafter stated by reason of having been in charge of this case and the trial thereof before the Court and a jury November 19 and 20, 1974.

2. I submit this affidavit in opposition to the Motion for Costs by defendants Herbert S. Cannon ("Cannon") and Cannon, Jerold & Co.

3. It is submitted that this Court should defer consideration of the motion pending the determination of the appeal which will be made herein as soon as Judgment is entered, even if it were deemed that the Court retains jurisdiction of this motion during the pendency of the appeal.

4. The affidavit of Steven H. Thal, Esq. sworn to November 27, 1974, submitted in support of motion completely misconceives the nature of the case and treats the Federal

Securities Laws claims as frivolous. On the contrary, such claims were maintained throughout the trial and the federal violations were the means whereby defendants knowingly procured the breach of trust by the double fiduciary who was both an agent and a director.

5. Defendant Cannon was the actual, physical conduit of monies to defendants Rittmaster and Lawrence who received unsecured personal loans as a result of inducing the purchase of a certificate of deposit in the Bahamian bank.

6. Defendant Cannon had actual knowledge of this passage of money and actual knowledge of the fiduciary relationship. Once it was proven that the certificate of deposit was in fact purchased in a foreign bank, it was then the burden of defendants to show that under one or another provision of federal securities laws that registration was not required. In view of the dismissal at the end of the plaintiff's case, defendants did not even attempt to carry their burden of showing an exemption under the statute. It was admitted that the certificate was unregistered.

7. While this motion is not the place to argue the merits of the appeal, it is appropriate on this motion to point out that the exhibits show that Cannon not merely put up the $100,000 money for *stockholders* to purchase the whole bank, but he promptly turned around and pulled that amount of money out of the *bank itself,* thereby looting the bank, and purchasing the cow with her own milk.

8. Subsequent thereto, he was able to itemize and analyze the bank's entire assets on three handwritten sheets of paper in evidence (only partially filled with writing), and

with a straight face perpetrate his Ponzi-type scheme, corrupting agents with full knowledge that the "Bank" was nothing but a small upstairs safe, and that its corporate being could be encompassed in three pages of scribbling.

9. Under these circumstances and where the alleged securities laws violations were the means and form of causing breaches of duty, it is submitted that it is wholly inappropriate to consider awarding counsel fees or any other costs against the plaintiffs.

Accordingly, it is respectfully submitted:

(a) that consideration of the motion for costs, even if the Court has jurisdiction thereof, should be deferred until completion of the appeal; or

(b) the motion should be denied forthwith.

/s/ CLENDON H. LEE
Clendon H. Lee

(Sworn to December 12, 1974.)

Transcript of Testimony

[1]

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

73 Civ. 4890

AID AUTO STORES, INC.,

Plaintiff,

vs.

HERBERT S. CANNON, *et al.,*

Defendants and Third Party Plaintiff,

vs.

MURRAY KLEIN, *et al.,*

Third Party Defendants.

New York, New York.
November 19, 1974—10:00 A.M.
Room 102

Before:

HONORABLE IRVING BEN COOPER. *District Judge,*
and a Jury.

Appearances:

ROGERS, HOGE & HILLS, Esqs.,
Attorneys for plaintiff

Transcript of Testimony

CLENDON H. LEE, Esq.,
DOUGLAS I. MILAN, Esq.,
of Counsel.

KURZMAN & FRANK, Esqs.,
Attorneys for defendants and third party plaintiffs Rittmaster, Lawrence & Co., Inc., Arthur Rittmaster and Lee Lawrence

DAVID YAVARKOVSKY, Esq.,
of Counsel.

THAL & YOUTT, Esqs.,
Attorneys for defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

HARRY E. YOUTT, Esq.,
STEVEN H. THAL, Esq.,
of Counsel.

[2] (Jury duly impaneled and sworn.)

(Two alternate jurors duly impaneled and sworn.)

The Court: Your openings, counsel.

Mr. Lee: Thank you, your Honor.

May it please the Court—

The Court: Counsel.

Mr. Lee: Madam Forelady and members of the jury.

My name is Clendon Lee, as the Judge has told you, and Mr. Milan is going to be assisting me.

During the course of the trial some of the evidence we are going to put in is going to be pre-trial depositions,

that is where we examined people under oath in law offices, and I am going to ask Mr. Milan to pretend that he is the person whose deposition we have taken and he will sit up in the witness box there and will be reading and pretending that he is the particular witness and he will be asking him questions.

Now, our first witness will be the president of Aid Auto, Mr. Klein, who is here, and I will tell you very briefly about this case.

You realize that what I am telling you is not any evidence at all. It is my theory of the case on behalf of our client. As the Judge has pointed out to you, [3] you will listen to what comes out of that witness box and the pieces of evidence which we introduce, which is what you are going to make up your mind about, but what I am asking you in this opening statement to do, I am asking you to look out for what we think are the important things so that you will have them in mind.

When we finish with all of the evidence then we will make closing arguments for you and at that time I am going to ask you to call this situation exactly what we think it is. Very simply we are going to claim that this is commercial bribery.

Now, the Judge has told you about a certificate of deposit.

Aid Auto Stores, like any corporation or some individuals who have enough money, from time to time has money that isn't being used. They don't use it for inventory. Say it is the wrong time of the year. Maybe they just sold stock to the public, as was the case of Aid Auto, and they have some money left over, so they want to put the money to work. What do they do with it? If they have an ordinary checking account they don't get any

interest on that checking account, because that is known as a demand deposit.

In other words, you deposit one day, you draw a check on it and you take it out the very next day. You are [4] just demanding the money back from the bank. But if you have a so-called time deposit, that is that you agree with the bank that you won't draw it out for 30 days or 60 days or 90 days, what you do is you buy a certificate of deposit so that if you are a big steel company or somebody, and you see that you don't have to buy coal for the next 30 days, or iron or something, you tell your corporate treasurer, "Get busy and put that money to work."

Then you buy so many 30-day certificates of deposits, and some for 90 days and some for even six months, as was the case here. This was a six-month certificate of deposit. Aid Auto Stores sold some stock to the public and got in about $900,000. After they got that $900,000 in they had about $400,000 that they didn't need right away. So they took it to a New York bank here and they bought a $400,000 certificate of deposit. That was for several months, I think about three months, and when that certificate of deposit matured or ran off it became time for them to do something else with the money. They could either leave it at that bank and get a new certificate of deposit, or they could put it in a different bank.

One of the members of the board of directors of Aid Auto was a man named Rittmaster. Mr. Rittmaster used to have a stock exchange firm called Rittmaster, [5] Lawrence & Company.

Back in November 1972 Rittmaster, Lawrence & Company was an underwriter for some Aid Auto stock. By underwriter that means that they buy the stock from

Aid Auto and then sell it a higher price to the public. That is called a new issue of securities and Rittmaster, Lawrence was the underwriter, or the lead underwriter in that sale to the public.

That is where Aid Auto ended up with about $900,000 additional money for working capital.

One of the agreements—it is not at all unusual—in connection with that underwriting was that—first I will add one little thing here.

Among the underwriters, there were a group of Stock Exchange firms that sold this stock, but among the underwriters was a firm called Cannon, Jerold and Cannon, Jerold was the third largest of the underwriters in this group selling to the public. When things are sold to the public it is sold pursuant to what is called a prospectus. A prospectus is a booklet which has been filed with the Securities and Exchange Commission and after a while it becomes effective. That is the language they use. You are then permitted to sell to the public after that prospectus, which is a part of the so-called registration [6] statement, becomes effective. But we are not suing under the registration statement.

All this is by way of background.

On the face of that prospectus of which defendant Cannon, Jerold, which the defendant Mr. Cannon was a principal, right on the face of that prospectus it says that Rittmaster, Lawrence & Company were going to get in addition to the underwriting commission, the profit they make selling to the public, they were going to get $44,000 payable in advance after this public offering to be a financial consultant to Aid Auto Stores for two years, and that Rittmaster, Lawrence & Company would also

have the right to designate a member of Aid Auto Stores board of directors.

Now, the board of directors of a corporation, as you know, manages the corporation and elects the officers. So a member of a board of directors is an important job.

Now, this public offering took place at the end of November 1972. In December of 1972 the consulting agreement was entered into between Aid Auto and Rittmaster, Lawrence designating Rittmaster, Lawrence the financial consultant and advisor for Aid Auto in the future, and in January 1973 Mr. Rittmaster was made a member of the [7] board of directors of Aid Auto. All as set forth right on the face of this prospectus, the same prospectus that defendant Cannon, Jerold had to do with as the third largest of the underwriters.

Then what happened? Well, we reach about April 1973 and Mr. Rittmaster, the financial consultant and member of the board of directors, is consulted as to what to do with this $400,000 that is running off. He says, "Well, I think we ought to spread it around and not leave it in the bank. It will help the company." And so on.

"Put a couple of hundred thousand in a New Jersey bank and a couple of hundred thousand in the same New York bank and a hundred thousand in the certificates of deposit in the Atlantic & Pacific Bank of the Bahamas.

So Aid Auto turned around and put $100,000 in the Atlantic-Pacific Bank of the Bahamas. They tried to do it early in April, but apparently the check wasn't cashed, so they issued another check and that check was handed over in Mr. Rittmaster's office to a Mr. Schweitzer, who was supposed to be the head of the Bahamas Bank, and at the same time Mr. Rittmaster and his partner, Mr. Lawrence, signed notes for $25,000 to the Bahamas Bank

and a couple of weeks later or so two checks in the amount of $25,000 each were sent from the Bahamas Bank to Mr. Cannon and Mr. Cannon turned [8] them over to Mr. Rittmaster and Mr. Lawrence.

Now, what is the picture there? It means that these two notes were for unsecured personal loans. It means that a man who was a director of the corporation, Mr. Rittmaster, and his partner, Mr. Lawrence, who together were the financial advisers and had advised the making of this deposit in the Bahamian Bank, it means that they were doing something for their own personal benefit.

Who knew that they were doing it for their own personal benefit? We say that Mr. Cannon knew it. The evidence will show that Mr. Cannon met with Mr. Rittmaster back in December. He had known Mr. Rittmaster for a long time, while he hadn't had much to do with him in recent years. His firm had been the third largest underwriter in this group and as the third largest underwriter he knew what was in that prospectus. He knew that Mr. Rittmaster was a member of the board of directors and he knew that Rittmaster, Lawrence was financial consultant to Aid Auto. He talked along—and the evidence will show that he met with Mr. Rittmaster and Mr. Lawrence over the next few weeks and that he knew that the Bahamian Bank was going to make these personal loans when the certificate of deposit was bought.

Now, how does Mr. Cannon also get in here? Mr. [9] Cannon was a promoter of the Bahamian Bank, the Atlantic-Pacific Bank. He wanted its deposits to grow because if its deposits grew the bank would then have more assets to lend out and presumably could make money. Mr. Cannon was in at the birth of this bank, which wasn't

very old. He had been down in I believe it was March, March of 1973, just a few weeks before this certificate of deposit was there. He had gone up in the second story of this building where the bank was. He had looked at the bank records. He had looked at the safe up there where the bank records of bank assets were kept.

He knew what the bank's assets were. He knew that Mr. Rittmaster and Mr. Lawrence owed a duty of absolute undivided loyalty to Aid Auto. He knew that they were going to get these unsecured personal loans. He also knew that an employee of the Rittmaster, Lawrence firm, a fellow named Iwanier, was going to get a commission on this amount and he had written a letter to Iwanier confirming that he would get a commission on all deposits obtained. So that Mr. Cannon, according to our interpretation of these facts and the interpretation which we will ask you to make on it after you have heard all the evidence and our final arguments and the Judge has charged you as to what the [10] law is, the interpretation that we want you to place upon these facts is that this was a case of out and out commercial bribery.

If you haven't guessed the end of the story, obviously the Bahamian Bank fell apart. We discovered in August for the first time—August of 1973. Mr. Murray Klein, the president of Aid Auto, finally reached the fellow on the telephone down in the Bahamas and he said, "We want to get our money back and we want to get it back in a hurry."

He for the first time learned about these personal loans made to these two insiders then. He called a little bit later in August says, "Where is my check?"

"We will waive the interest and we will even give you 1 per cent, but where is my check? I want nine thousand back. Where is my check?"

They said, "The reason you haven't got your check, Mr. Klein, is that you are not going to get your check until Mr. Rittmaster and Mr. Lawrence pay off their own loans."

Shortly thereafter the Bahamian authorities closed down the bank. We haven't got any part of our money back. We are also suing for something else. We are suing for that $44,000 that was paid in December 1972, and we are asking [11] Cannon and Cannon, Jerold not only to pay us the $100,000 of the certificate of deposit on the ground that they corrupted our director and our agent, but we also say that they deprived us of the valuable services of these people which we paid for in advance to the extent of $44,000, and we want that back, too.

We also want back—we don't know exactly whether it is $2000 or $1500, which was paid to Mr. Iwanier or on his behalf to the Rittmaster, Lawrence firm in connection with obtaining this. So we want these three things. We want our bait back, if you can call $100,000 bait. We want the $100,000, we want the $44,000 and we want the commission, which was either $1500 or $2000, I am not sure which, and I am not sure the evidence will be clear on that, but we will take the one thousand five, if that is satisfactory.

That's it in a nutshell. I know my adversary, who I have only met for the first time in this case, has a different interpretation of the facts and I know you can make up your own minds after you heard the witnesses on the stand.

As I told you, one of the witnesses will be my associate, Mr. Milan, who is playing the role of some of the witnesses whose testimony has already been taken under [12] oath and we will put it in that way.

Thank you very much, your Honor.

The Court: Mr. Youtt.

Mr. Youtt: With the permission of the Court and in the interest of clarity, I would request the opportunity of delaying making the opening statement until the opening of our case after the plaintiff has rested. I feel that, I will be able to present a clearer picture of the somewhat complex fact situation at that time than I would at this time, and I would request permission to do it in that fashion.

The Court: I am going to deny the application and tell you to go forward at this time, and I will seize upon your own words just now, complex, to indicate why it was that the Court felt that those two persons on the jury were not suitable for this particular case.

Please proceed, Mr. Youtt.

Mr. Youtt: Thank you, your Honor.

Ladies and gentlemen of the jury, I recognize at the outset of this case that you are going to be called upon to make some important factual conclusions and decisions in an area of life which you are not on a day-to-day basis involved with as the professional investors and professional people who will probably be witnesses in this [13] case are.

I recognize that, but nonetheless I trust your judgment as fact finders in a case such as this, and there are important facts to be drawn in this case.

As the Court has instructed you, Mr. Cannon and Cannon, Jerold are the only people who you are to be concerned for reaching your conclusion and are charged with what Mr. Lee has described to you as being commercial bribery. Words having criminal import in another context, but words about which you are asked to draw civil conclusions in this case. You are asked by the plaintiff, if the plaintiff is to recover on its theory of commercial bribery, to conclude that the defendant, Mr. Cannon, had knowledge that there was a specific fiduciary relationship

—and by fiduciary I mean a close relationship of trust between Mr. Rittmaster—who I don't think there will be any doubt betrayed duties to Mr. Klein and his firm, Aid Auto Stores, but what you are asked to decide with respect to Mr. Cannon is that Mr. Cannon knew that there was a relationship between Mr. Rittmaster and Aid Auto Stores, that knowing that and knowing further that the bank in the Bahamas, which is the subject of this lawsuit, was a bad bank, went to Mr. Rittmaster and his firm, and induced them to do something [14] against the interest of Aid Auto Stores with that specific intent and with that as a device or a scheme or a plan in order to, in effect, defraud Aid Auto Stores.

Those charges, ladies and gentlemen, the defendant Cannon and Cannon, Jerold strenuously deny.

I suggest to you, ladies and gentlemen, that if the evidence is as it has been suggested by Mr. Lee, and that is all that the evidence is, there isn't sufficient evidence even to draw the inference, but if there ever comes a time when you feel there may be inferences that can be drawn I ask that you keep an open mind in this case in order that you can hear from our side, the defense, exactly what the situation was and I again am going to tell you briefly my interpretation of the facts as I see them, having prepared for this case, but cautioning you as Mr. Lee did that I am not testifying, I am not here to present evidence. I am here to present a theory of the case and based upon the evidence to argue to you, in effect to present you with a theory which you can either accept or reject based upon what you draw as facts coming from the witness.

Now, the facts as the defendant will present them are as follows:

Mr. Cannon, is an investor. Mr. Cannon is an investment specialist. He is a broker. He has been in [15] the stock brokerage business for a substantial part of his life.

In connection with that business he met a man by the name of Mr. Schweitzer, Moris Schweitzer. If you see the pleadings in this case, he was named as a defendant, but not ever served. Mr. Schweitzer was involved some time ago, a couple of years ago or a year or so ago, in the possible purchase of a bank in the Bahamas. Mr. Cannon had met him before. Mr. Schweitzer approached Mr. Cannon about possibly raising some money for that bank. Mr. Cannon assisted Mr. Schweitzer in the initial startup of that bank.

As in all of these kinds of ventures they involved dreams of success, hopes of success, projections of success. With those projections and dreams Mr. Cannon supported Mr. Schweitzer. That financial support came to an end in that Mr. Cannon was repaid early in the investment by Mr. Schweitzer and the bank.

However, Cannon continued to have an interest in the success of that bank. Some time in December of 1972, as these things happen in investment circles, people who are investment specialists get together to discuss what is going on in their respective areas. Mr. Cannon and Mr. Rittmaster had been partners years ago. They haven't [16] seen each other for quite some time. In fact, there had been a falling out long ago between them and they really hadn't had any contact, but in December, at the instance of Mr. Rittmaster's partner, Mr. Lawrence, who was also named as a defendant in this case and as a member of the firm Rittmaster, Lawrence who represented the plaintiff as financial advisors. Mr. Lawrence called upon Mr. Cannon in December.

Now, I think the evidence will show that this was prior to the time that Mr. Rittmaster became a director of the board of Aid Auto Stores. They got together and discussed the financial world in general and what they were doing. It was a bury-the-hatchet kind of a conference where they were exploring the possibility of doing business together again as investment specialists. Not in any formal relationship, but just in terms of context.

During the course of that December meeting Mr. Cannon, in discussing numerous things that he was involved in, said, "There is a bank in the Bahamas that wants to build up deposits, the idea being that if you can build up deposits you can build up a source of funds so that you can provide money to loan out to various ventures so that you can become a success as a bank."

One of the advantages of the Bahamas is that [17] it is available not only to local funds, but primarily it is available to what the investment people called offshore funds, and that is one of the shorthand words that means funds invested from foreign sources. That was the attractiveness of that type of a venture.

Mr. Cannon said they are looking to build up deposits.

Now, the evidence will show, primarily from the testimony of Mr. Cannon, Mr. Cannon did not know at that time that Mr. Rittmaster was to become a director in Aid Auto Stores, nor did he know that Rittmaster, Lawrence & Company were becoming or in the stage of becoming investment advisors to Aid Auto Stores.

As a matter of fact, Mr. Cannon's firm, Cannon, Jerold & Company was what they call a sub-underwriter, one of the assistant underwriters, so to speak, to Rittmaster, Lawrence in the public issue of Aid's stock. A public

issue, as I think Mr. Lee will probably bring out, involves what they call going public and issuing stock and underwriting it through numerous firms.

Now, those are true facts, but Mr. Cannon was only one of a number of men in his firm and he didn't have specific knowledge of the contents of every prospectus that comes into his office or that his office is involved in, [18] and he did not acknowledge that Aid Auto Stores and the Rittmaster firm had any close relationship at that time. I think the evidence will show that the Aid Auto Stores were not even discussed in December of 1972.

We go on now into the months of January, February and March 1973, bearing in mind that the date that the certificate of deposit was purchased by Aid Auto Stores was approximately April 12 or 13 of 1973. During that time on numerous occasions, most of which were instigated either by Mr. Lawrence—usually Mr. Lawrence of Rittmaster Lawrence—or Mr. Rittmaster. Mr. Cannon had some contact with the Rittmaster, Lawrence firm. One of the things that he was interested in and one of the things that had its genesis back in November of 1972 was the possibility of attracting—again I will use the shorthand word—offshore funds from foreign sources for the bank. Mr. Cannon at that time will testify that he believed the bank could become a success.

Based upon his knowledge of the bank he thought things would be going well; that it was a good idea to start a bank there and that it was a good idea to back that bank.

But he will testify that his interests or one of his primary interests in the Rittmaster, Lawrence firm was [19] the fact that the Rittmaster, Lawrence firm had been involved in offshore investment activities, not specifically the Rittmaster, Lawrence firm, but specifically one member

or one man who worked for that firm, a man by the name of Mr. Iwanier, who also is named as a defendant in this case, but was not served by the plaintiff.

Now, Mr. Iwanier was a person again who became engaged in the activities of the bank from the standpoint of his own investment specialty, attracting funds for banks and did an inquiry. He investigated the bank on behalf of himself and on behalf especially of Rittmaster, Lawrence.

Mr. Cannon's function in this matter, as the defendant's testimony will present to you, was merely to introduce Mr. Rittmaster's firm, who he felt to be specialists in the area of providing offshore investments for banks, to the bank.

What he did was he said to Mr. Rittmaster and he said to Mr. Lawrence, in effect, "Get in touch with the bank. If you are interested in this as a possible venture to utilize in your own investment specialty, get in touch with the bank. Here is the name of the president, Mr. Schweitzer. You can call him at any time. They are interested in obtaining deposits. They will be happy to talk to you."

[20] I believe the evidence will show, ladies and gentlemen, that that is exactly what Mr. Rittmaster did, that Mr. Rittmaster, Mr. Lawrence and Mr. Iwanier had numerous direct contacts with the bank, with Mr. Schweitzer during the period January, February and March of 1973.

Now, I believe also that the evidence will show that probably at that first meeting between Mr. Rittmaster and Mr. Lawrence and Mr. Cannon that the discussion went to the area of, Number 1, what kind of commissions are available for generating these funds, because, after all, that is what investment specialists receive some of their pay for, that is finding money, matching people who need money with people who have money so that both can profitably gain from it.

Investment specialists very frequently obtain fees for that service. So one of the subjects of discussion I think at that first meeting—certainly at one of the early meetings —was the possibility or what were the possibilities for income for the Rittmaster, Lawrence firm.

Again, they were in that business. It was a legitimate subject of discussion. Mr. Cannon indicated that commissions would be available. Then upon the question of Mr. Rittmaster, "Would we be able to borrow money from the bank—we as individuals, assuming that we were able [21] to generate deposits," Mr. Cannon answered something generally to the effect, "If you produce for the bank or if you provide deposits in the bank, certainly that is a possibility. Get in touch with Mr. Schweitzer."

Now, ladies and gentlemen, Mr. Lee might have you believe that something like that is a very sinister sort of a thing.

I suggest to you, ladies and gentlemen, that in banking circles that very often is the way loans are obtained, that banks especially banks such as the bank in the Bahamas are not equipped to just all of a sudden draw out of their cash drawer thousands and thousands of dollars and that sometimes in order to issue a loan they request that people obtain certificates of deposit as not exactly collateral, but in order to provide the liquid funds to present the loan.

So it was a general discussion not aimed at anything, not really aimed at attracting Rittmaster, Lawrence as sellers of the bank or as promoters of the bank's deposits, but just a general financial discussion, again not aimed at Aid Auto Stores in any way.

As the months January, February and March came by other discussions took place on infrequent bases and involving numerous areas of investment interests between

[22] the Rittmaster firm and Mr. Cannon. On one of these occasions Mr. Rittmaster called Mr. Cannon and said to the effect, I am very good friends with the president of Aid Auto Stores, who have recently gone public. I am close with him. I am wondering. If I am able to place a certificate of deposit with them with the bank, the Bahamas Bank, would I be able to get a loan for myself and my partner?

Mr. Cannon didn't think about it at any great length, but said, "I don't know. I think you ought to take that up with Mr. Schweitzer. I don't see why not."

Either Mr. Cannon mentioned it to Mr. Schweitzer, because he was in touch with Mr. Schweitzer on occasion, or Mr. Rittmaster got directly in touch with Mr. Schweitzer of the bank concerning this matter. The fact is that at the time the certificate of deposit for $100,000 was placed with Aid Auto Stores, loans were made to Mr. Rittmaster and to Mr. Lawrence personally for $25,000.

Now, it is that subject, ladies and gentlemen, which becomes an issue to this case. Did Mr. Cannon by the limited role which he had—and incidentally, I will point out that at the time that the payment of the funds which was made the checks that were issued, the checks were issued for those loans as Mr. Lee stated. The checks were [23] sent to Mr. Cannon. I am not exactly sure why that was. Maybe Mr. Schweitzer considered him one of the few people that he knew or one of the people that he dealt with in New York before, that he had dealt with him on a more lengthy basis than he had with Mr. Rittmaster or Mr. Lawrence.

The fact is, as Mr. Cannon also recalls it, the notes themselves had not been signed by Mr. Rittmaster and Mr. Lawrence. Mr. Schweitzer was sending the checks together with the notes to be signed by Mr. Rittmaster and Mr.

Lawrence and this is possibly why he sent it to Mr. Cannon. There was no pre-arrangement, as Mr. Cannon will testify, that those loans were sent to him.

Now, the issuance of those loans, to this director Mr. Rittmaster, who was also serving as the investment advisor, is the issue that will present you with numerous fact questions.

Mr. Lee has stated to you, ladies and gentlemen, that at that time there was an absolute duty of undivided loyalty existing in Mr. Rittmaster which made that the acceptance of that loan a wrongful act in his capacity as director of Aid Auto Stores.

I take issue with that, ladies and gentlemen. I think under the facts and circumstances as you will see that they occurred in this case, that's true, because Mr. [24] Rittmaster received that loan and Mr. Lee Lawrence received those loans without disclosing to Aid Auto Stores the fact that they had done so and without disclosing to Aid Auto Stores that they, their firm had received a commission of 1½ per cent on the sale of that certificate of deposit.

But I am telling you, ladies and gentlemen, and I believe the Court will instruct you as a matter of law, that it would have been possible for them to have received those benefits —for them, Rittmaster and Lawrence to have benefited from that transaction in just the way that they were and have done so legally consistent with their duties to Aid Auto Stores, and that is if they had disclosed the fact that they were receiving those loans and the fact that they were receiving a commission for this transaction.

I am going to argue to you, ladies and gentlemen, as a matter of fact that when we are dealing with corporate directors, a corporate director in this case who has—if I may use the symbolism—more than one hat. He has his

hat as a director of Aid Auto Stores, but at the same time he doesn't relinquish his hat as an investment specialist, as a man in the business of generating investments for people who need money. He doesn't relinquish that hat at all. The law provides specifically for that combination of hats, so that we may have directors sitting [25] on two boards of two companies who are dealing with each other at the same time, so long as the boards of both companies know.

Mr. Cannon will testify, Number 1, that he assumed at all times that Mr. Rittmaster—at all times that Mr. Rittmaster dealing with Mr. Klein, as he said it as a friend, would have disclosed those facts, that certainly when he learned that Mr. Rittmaster was a director, that was assumed that that was Mr. Rittmaster's duty, and further that if we look in the prospectus itself that Mr. Lee seeks to rely upon, that this prospect of Rittmaster as a director and Rittmaster, Lawrence, his firm, receiving commissions for other work that they would do on behalf of the Aid Auto Stores was specifically set forth. In other words, this was a kind of relationship where it was assumed that Mr. Rittmaster would benefit from his position and so long as he disclosed it that would be perfectly all right with Aid Auto Stores.

I am suggesting to you, ladies and gentlemen, that as a matter of fact when you are called upon to decide the very important issue, Mr. Cannon's very future, as to whether or not he committed commercial bribery as Mr. Lee has determined on his own initiative to interpret the fact, [26] you should consider very strongly what duties Mr. Cannon had and what Mr. Cannon could reasonably suspect a person who he thought to be an honorable man, Mr. Rittmaster,

would do with respect to any duties that he may have to someone else as a fiduciary, as a person in a position of trust.

Ladies and gentlemen, I suggest to you that at the close of this case on the issue of commercial bribery, which Mr. Lee has presented to you, you will not be able to find by a preponderance of the evidence that Mr. Cannon or Cannon, Jerold bribed anybody. For the life of me I don't know why he is here to answer to those charges, but he is because he has been sued and you, ladies and gentlemen, must decide those factual issues which are presented to you.

Now, there are other issues which were presented under the Securities Laws, ladies and gentlemen, which also raise issues of fact which will be presented to you. Mr. Lee has not argued them and I don't know exactly what he intends to do with them in this case, but at such time as he does present them I will be able to have a chance to address you at the close of this case and present my views as to them.

I feel, and again this is my feeling in this case, that you will find that those cases are [27] equally—that those charges are equally ill-suited to the facts of this case, and will have no difficulty in rendering a verdict for the defendant on all counts.

Thank you.

The Court: Call your first witness, Mr. Lee.

Mr. Lee: Thank you, your Honor.

The plaintiffs call Mr. Murray Klein.

Murray Klein, called as a witness by the plaintiffs, having been first duly sworn, was examined and testified as follows:

The Court: Mr. Klein, you are about to give testimony under oath, and I say this to all witnesses in order to avoid an outburst that may cause a mistrial. You will just answer the question that is put to you. You are not talking in your office or outside the courtroom. There are certain rules of law that demand that a Judge confine a witness to the questions put to him. You are not to volunteer any testimony. Wherever you can answer yes or no, you will do exactly that.

Do you understand that?

The Witness: I do, sir.

The Court: Will you be good enough, Mr. Lee, will you pull that lectern all the way back because the [28] acoustics are very poor in here.

Direct Examination by Mr. Lee:

Q. Mr. Klein, what is your occupation? A. I am the president of Aid Auto Stores.

Q. And Aid Auto Stores is the plaintiff in this action? A. Yes.

Q. How long have you held that position? A. Well, it is a two-fold setup.

The Court: No, how long have you held that position, please?

A. Thirteen years.

The Court: Next question.

Q. Will you state your business background briefly. A. Well, I have been in the automotive business for the past

36 years, during which period of time I was a salesman for a wholesale firm. I had a retail automotive store which I ran for myself and since 1961 I have been employed by Aid Auto in its administrative area.

Q. Will you describe the business of Aid Auto Stores as it existed in November 1972 at the time of your public offering? A. Aid Auto consisted at that time of 60 franchised [29] retail automotive stores in the New York area. It consisted of 14—I am sorry, of 11 company-owned stores in Florida, Miami and Dade County in Florida.

Q. What was the purpose, in general terms, of the public offering of the stock of Aid Auto? A. Principally we were on an expansion program of opening up more units and possibly looking for acquisitions in the retail and possibly wholesale automotive area. This was the basic reason.

Q. I wonder if you would go into a little detail, if you will, about how Aid Auto Stores came about and the detail of its business in a sense so that we can understand just exactly what type of an operation it is. A. Well, Aid Auto was formed in late 1953 and early 1954, as a buying cooperative for 27 independent automotive dealers in the metropolitan area. They found that through their united efforts of buying collectively and formulating an advertising program through the New York newspapers they would be in a better position to compete with the larger chains that were in existence at the time.

The Court: In the sale of?

The Witness: Automotive parts and accessories.

The Court: By "automotive parts and accessories," give us some examples. These people may know it and they [30] may not know it. Some may drive a car and others may not.

The Witness: Tires, batteries, spark plugs, floor mats, mirrors, ignition parts and the like, your Honor.

The Court: Thank you.

Q. What was your relationship to Aid Auto at that time? A. Well, at that time I was one of the dealers instrumental in helping to formulate the organization and although I retained my unit, my store, which was in Jackson Heights, I was at that time the unpaid president of Aid Auto Stores and I helped formulate much of the policies which it used.

Q. Did there come a time when there was a change in the manner in which the business was carried on? A. Yes. We found that there was a growth in the company itself and in 1966, I believe it was, the original charter members decided that we would try to franchise other independent dealers or those who were desirous of becoming a part of our industry and license them under a franchise arrangement using the name of Aid Auto Stores.

Q. When did that take place? A. In 1966.

Q. Was that carried out? A. Yes, it was.

[31] Q. From 1966 up until the time of your public offering would you describe the further developments in the company if any?

The Court: I wonder why we need all of this. This gentleman says that he has been identified with the company from its very inception. He shows us that he occupied a top executive post. He took under advisement and he controlled to a certain extent its policy. He has familiarity with its affairs. What more do you want?

Nobody contests that the plaintiff corporation had a right to make this particular purchase of a certif-

icate of deposit. You have a man here who has been around. I don't know what other detail you need for this particular transaction. That is the way it strikes me.

Mr. Lee: Thank you, your Honor.

Q. In 1972, at the time of your public offering, about what was the size of the Aid Auto business in volume of sales? A. Well, we had absorbed a chain in Florida in May of 1972. This consisted then of seven stores and I believe our total volume combined was in the area of six or $6.5 million annual sales.

Q. Prior to the time when Aid Auto went public with its sale to the public—I am talking about in 1972—[32] had you had, and by you I mean you yourself individually, had you had any dealings with investment banking and the issuance of stock and so on by the corporation?

The Court: At the corporate level?

Q. Yes. A. No, sir.

Q. As the president and chief executive officer, would you describe the nature of your duties?

The Court: As at what time, Mr. Lee?

Mr. Lee: In November 1972.

The Court: Yes, sir.

A. I would assume it would be all of those germane to the post of president. I was an active president. I actually ran the merchandising programs of the company. I was involved in the financial problems, although I did have an officer manager. I took my place where it needed to be in

the area of personnel. I basically kept my finger in most every part of the running of the corporation.

Q. Approximately what was the number of employees of the corporation at that time? A. Well, in New York we had approximately 45 people and in Florida we had approximately 40 or 45. In the New York area, of the 60 units which we were running only two were owned by the parent company under subsidiaries. The [33] other 58 were independently operated and their personnel naturally were not ours.

My personnel were principally those within my warehouse or within my sales area within the New York territory.

Q. Mr. Klein, I show you a booklet entitled "Prospectus, Aid Auto Stores, Inc." and the very bottom line on that front page is the sentence, "The date of this prospectus is November 30, 1972," and ask you whether that is the prospectus under which the shares of Aid Auto were sold to the public.

A. Yes, it is, sir.

Mr. Lee: I offer it in evidence.

The Court: Any objection?

Mr. Youtt: No objection.

The Court: It is received and mark it in evidence.

(Plaintiff's Exhibit 1 was received in evidence.)

The Court: In matters of this kind, the Court expects there will be a stipulation of proof by the attorneys so as to obviate the necessity of going through a lot of testimony and wasting everybody's time. These are things that you must agree on or you should agree on, so as to [34] curtail the

amounts of time spent. A thing like this last item should have been agreed on and it could have easily been agreed on by counsel without putting any questions at all.

Now let's go forward.

Mr. Lee: Thank you, your Honor.

Q. I ask you to look first the bottom of the page where it says "Rittmaster, Lawrence & Company, Inc."

Now, Rittmaster, Lawrence & Company were the underwriters of this issue, were they not? A. Yes, they were, sir.

Q. What did that mean to you, what their function was? A. In this particular area I felt it was their position to merchandise, sell the issue or the number of shares which we were offering to the public on the issue date.

Q. What was the number of shares that you offered to the public? A. I believe it was 496,000.

Q. I now ask you to look on Page 20 and Page 21 of the prospectus. Do you see the caption "Underwriting"? A. Yes.

Q. Under that caption—and if I may, your Honor, I am going to read out loud the list of certain of the [35] underwriters.

The Court: I think all you need to do, since it is in evidence, Mr. Lee, is just read it to the jury. It is in evidence. You don't have to ask him.

Mr. Lee: Very well. I don't believe I have to ask questions about it.

The Court: Just read whatever parts of the document you wish to the jury. It is in evidence.

Mr. Lee: I am reading on Page 20 and then onto Page 21, of this prospectus under the caption "Underwriting."

(Mr. Lee read to the jury from Plaintiff's Exhibit 1 in evidence.)

The Court: Do we need all of those people?

Mr. Lee: I am getting down to Cannon, Jerold.

The Court: Then go right to it. There is a list and about how many names are listed there, Mr. Lee, approximately?

Mr. Lee: There are 13 underwriters listed.

The Court: Thank you. And among them is Rittmaster, Lawrence?

Mr. Lee: Rittmaster, Lawrence is the lead underwriter.

The Court: And what number is Cannon, Jerold?

Mr. Lee: Cannon, Jerold, opposite which is [36] listed 15,000 shares, and I believe it is the third largest.

The Court: How do you figure it?

Mr. Lee: I was going to read the list. There was one of 30,000, the Seaboard Funds, and the next in line is Cannon, Jerold at 15,000.

The Court: Okay, sir. Very well.

I think at this juncture we ought to let the jury go because I have a couple of legal questions to take up with you and we will continue with the resumption of testimony at two o'clock promptly. Be ready to go in that box at two o'clock promptly.

Mr. Clerk, will you excuse the jury. Counsel will remain with me. Mr. Klein, you might as well step down because your testimony will be continued at two o'clock.

Excuse the jury and remember what I said about talking about the case, ladies and gentlemen.

All rise.

Murray Klein—for Plaintiffs—Direct

(Jury left the courtroom.)

The Court: There is a motion pending before us to strike the jury demand. I am taking it up at this hour, because, Number 1, I didn't want to keep the panel of jurors waiting unnecessarily, unnecessarily, I say, because last week at a conference I indicated that the [37] defendant under law was entitled to a jury and Mr. Lee took the opposite position, and since our discussion in chambers Mr. Lee brought on the motion to strike the jury demand asserted on behalf of the defendants, and I would like to at this time deal with that motion.

The motion is denied in all respects. It is a motion submitted to this Court on the eve of trial and the motion, as I have indicated, is to strike defendant's jury demand pursuant to Rule 39A of the Federal Rules of Civil Procedure.

Plaintiff Aid Auto asserts five claims against defendants Cannon and Cannon, Jerold in this action. The first four claims are automatically related to violations by the defendants of the Federal Securities Laws. A jury trial is appropriate in a damage action alleging violations of the Federal Securities Laws. (Hohmann vs. Packard Instrument Company, 471 Fed. 2d 815, Fifth Circuit, 973; Dasho vs. Susquehanna Corporation, 461 Fed 2d 11 at 24, Seventh Circuit, 1972.)

In the fifth claim, plaintiff Aid Auto asserts against defendants Cannon and Cannon Jerold that these two defendants induced a breach of loyalty on the part of Rittmaster and Rittmaster, Lawrence & Company to plaintiff Aid Auto.

[38] Plaintiff has made out no charge of fiduciary obligation on the parts of Cannon and Cannon, Jerold.

Although an action directly against a director would warrant an equitable action tried without a jury, here where the action is against a third party —and we emphasize third party—defendants here, where the relief sought is money damages and where the plaintiff has proven no fiduciary obligation on defendants' part, the case should be tried to a jury.

(See Kaminsky vs. Kahn, 20 NY 2d 573, 1967.)

Off the record now.

(Discussion off the record.)

(Luncheon recess.)

[39] AFTERNOON SESSION

2:00 P.M.

(In open court; jury present.)

MURRAY KLEIN resumed.

The Court: Please resume.

Direct Examination by Mr. Lee (continued):

Q. Mr. Klein, after the company received the proceeds of the underwriting of the common stock, what did the company do with those proceeds? A. We used a portion of it to pay off the costs of preparing for our issue and after utilizing some of the dollars we found that we had $400,000 of moneys which we did not need at the particular time. It was determined that we deposit those funds in

certificates of deposit and it was so done with the National Bank of North America.

Q. Approximately when were those certificates of deposit made or purchased? A. I believe it was either late December or early January. Late December '73—'72 or early January '73.

The Court: May I interrupt?

Mr. Klein, when you say we, I presume you mean you and the board of directors.

The Witness: Yes, sir.

The Court: What advantage did you people see [40] particularly in the purchase of the certificates of deposit as against any other arrangement that you could make with regard to return on your money? Why did that particularly appeal to you and the board, is all I want to know.

The Witness: Well, your Honor, for one thing, it was a short term investment. It was a 90-day investment. I believe it was mentioned before we were on an ongoing program of acquisition and expansion of the company. We didn't want to tie up our funds for too long a period.

The Court: Thank you, sir. That is an answer. Next question.

Mr. Lee: I would like to read at this point from Exhibit 1, the prospectus, some language which appears on the bottom of the first page.

(Mr. Lee read further from Plaintiff's Exhibit 1 in evidence to the jury.)

The Court: May I with great respect and without attempting to criticize, if there is anything which

shows the need of a jury that has had more than just the menial jobs in life to sit as ministers of justice, it is the reading by Mr. Lee. That is so complex that I just managed to wade through it and I have considerable doubt—and I don't know what the purpose of giving that to the jury [41] at this particular time is.

If you want to bring out some evidence that elucidates that and then read it as a consummation of what has been developed if it should so prove to be, that is another matter, but taking it out of a clear sky and loading us with it is almost meaningless, Mr. Lee, until you have developed something that warrants it and makes it much more understandable.

That language is heavy.

Mr. Lee: I agree, your Honor, it is heavy, and if I may, I will interrogate the witness now about what I just said.

The Court: You should have done that first. You are putting the cart before the horse.

All right.

Q. Mr. Klein, who was the representative referred to in the language which I just read to the jury? A. Arthur Rittmaster of Rittmaster, Lawrence.

Q. It was Arthur Rittmaster's firm, Rittmaster, Lawrence that was to get a $44,000 consulting fee, is that correct? A. That is correct.

The Court: That is the way, sir. That is the way.

[42] Was it Rittmaster, Lawrence & Company which had the right to designate a member of the board of directors of Aid Auto? A. That is correct.

The Court: Don't you like that better?

Mr. Lee: I apologize to the jury for loading it on them so soon after lunch, your Honor, but I was afraid if I waited much longer it would be too late in the afternoon.

The Court: All right.

Q. Mr. Klein, was there a consulting agreement entered into with Rittmaster, Lawrence? A. Yes, there was, sir.

Q. When was that? A. That I believe was in December of 1972.

Q. Did a designee of Rittmaster, Lawrence become a member of the board of directors of Aid Auto? A. Yes, he did.

Q. Who was that? A. Arthur Rittmaster.

Q. When was it? A. In January of 1973.

Q. So that the stock offering took place November 30, 1972, and by January '73, both the consulting agreement [43] had been entered into and Mr. Rittmaster had become a member of the board of directors, is that correct? A. That is correct.

Q. Now, in connection with the certificates of deposit which you purchased—from what was the bank again? A. National Bank of North America.

Q. Did you consult or confer with Mr. Rittmaster in that connection? A. Yes, I did, and it was upon his—

The Court: Yes, I did.

Next question.

Q. What was the nature of that consultation? A. The disposition of the funds and it was upon Mr. Rittmaster's suggestion, approved by the board, that the four certificates,

each in the amount of $100,000 were purchased. They were purchased on 90-day term notes.

Q. After the purchase of those $400,000 of certificates of deposit, did you have any further discussions with Mr. Rittmaster as to the use of these liquid funds? A. Not until March of 1973, at which time they were coming up for maturity and we still did not have an area in which to use the funds and we therefore were trying to determine exactly what to do with them.

Q. What was that discussion with Mr. Rittmaster? [44] A. Mr. Rittmaster called me in the early part of March of 1973 and suggested that rather than concentrate all of our holdings in the one bank we spread it out, we dilute it and in that way put ourselves in a better bargaining position in the event that we needed larger sums of money for any need down the road.

He suggested that we deposit $100,000 in the New Jersey Bank of North America and $100,000 in the Nassau Bank. I have to go back a bit.

In October of 1972, Mr. Rittmaster had called me to suggest that if I could use another banking line he would like me to open an account with the Hempstead National Bank in Nassau County, New York.

Subsequent to that a Mr. Sullivan, who introduced himself as the manager of the bank, called me and I told him that if I had a need I would certainly utilize his services, but I never did.

At the time—

> The Court: I am sorry, but forgive me, Mr. Klein. I know you don't do it purposely, but I am going to strike the conversation you had with Mr. Sullivan. That is not the question you were asked. You were

asked about your conversation with Rittmaster. So the jury is instructed to disregard the testimony dealing with what Mr. Sullivan [45] had to say to Mr. Klein.

All right, go ahead, Mr. Klein.

Mr. Lee: Thank you, your Honor.

Q. Mr. Klein, prior to the public offering of November 30, did you have any discussions with Mr. Rittmaster with respect to banking relations of Aid Auto? A. Yes, I did, sir.

Q. What were those discussions? A. Well, he wanted to know which banks we were then utilizing for commercial purposes, and I told him, and he suggested that we open up a relationship with the National Bank of North America on 38th Street and Seventh Avenue.

I went to the bank with him and met one of the vice-presidents and we did open up an account there.

Q. Did you have any discussions with respect to any other banks with Mr. Rittmaster? A. Not at that time, no.

Q. When, approximately, did you open up your first banking relationship with the bank of North America? A. I can only pinpoint it. I believe it was some time in 1972.

Q. After that did Mr. Rittmaster mention the name of any other banks to you? A. In October of 1972 he mentioned the possibility [46] of opening an account with the Hempstead National Bank.

Q. Where is that? A. In Nassau County, New York.

Q. Now, in March of 1973, I was commencing to ask you about the conversations then that you had when the certificates of deposit were about to mature. Now, would you continue as to what your discussion was with Mr. Rittmaster? A. He said that he wanted us to put $100,000

in the National Bank of New Jersey, I believe it was, and $100,000 in the Nassau Bank without further identifying the Nassau Bank.

Q. Did he suggest letting $200,000 remain in the North American Bank? A. Yes, he did.

Q. Following that discussion with Mr. Rittmaster what happened? A. In the latter part of March or in the second or third week of March I was in Mr. Rittmaster's office with Mr. Eisenberg, the chairman of the board, and Mr. Rittmaster gave me two letters. I glanced at the top one. It was addressed to the New Jersey Bank and it requested that they issue us a certificate of deposit against the enclosed check of $100,000. I assumed that the second letter was [47] of like nature to "the Nassau Bank" in New York.

Q. The one in Hempstead, Long Island? A. Correct.

Q. Did you sign those letters? A. No, I did not. I put them in my—

The Court: No, I did not is an answer.

The Witness: I am sorry, your Honor.

The Court: Mr. Klein, let me tell you something. I am sure you are quite an active man in your business and I guess you know everything that goes on there all the way from the smallest item to the most expensive.

Well, in the law, and based on my experience at trial, there is nothing more staggering to lawyers on either side than when the witness says "no," or "yes."

The Witness: Thank you.

The Court: All right, go ahead.

Q. What happened to those letters? A. I took those back to my office and—

Q. From where? A. From Mr. Rittmaster's office back to my office. They were in my attache case. I opened them up and I found in fact that the second letter was addressed to the Atlantic & Pacific Bank & Trust Company, Nassau, Bahamas.

Q. What happened following that? [48] A. I immediately called Mr. Arnold Biegen of Booth, Lipton & Lipton, our corporate attorneys, and advised him that the bank in fact was Nassau, Bahamas and not Nassau, New York, as I had originally supposed.

Q. Did you have any further discussions with Mr. Rittmaster? A. Not at that time.

Q. When was your next discussion with Mr. Rittmaster? A. Well, I—

> The Court: Your next discussion with Mr. Rittmaster, as you best recall it, about when. That is the only question pending.

A. Relative to this matter?

Q. Yes. A. I believe it was in the ensuing days and I had informed Mr. Rittmaster that I was surprised to find that the bank was a Nassau, Bahamas bank, and that I was awaiting word from my legal department as to whether or not I should pursue the consummation of the deposit.

Q. Then what happened? A. A number of days later Mr. Biegen called and said that it was all right for me to make the deposit and so on April 3 I wrote to the Nassau, Bahamas bank, enclosed [49] the $100,000 check and request that they issue to me a certificate of deposit on a six-month term.

Q. When you said "issue to you," you mean issue to Aid Auto Stores? A. Yes, I'm sorry.

Q. Then what happened? A. On April 11, Mr. Rittmaster called me and asked what happened to the check. I said, "I mailed it out the 3rd of April and although I had not as yet received anything from the postal authorities that it had been received there, I assumed that it was in the Bahamas."

He then said, "I think you ought to put a stop order on that check."

In fact he said, "Mr. Schweitzer, the president of the bank, will be in my office on Friday, the 13th. Why don't you call the bank, stop the original check, draw a new check and I will send up a messenger on the 12th to pick it up and give it directly to Mr. Schweitzer."

The Court: The check you just mentioned was what particular check?

The Witness: The second check, your Honor.

The Court: The second check of—whose check?

The Witness: Aid Auto Stores.

The Court: In the amount of?

[50] The Witness: $100,000.

The Court: And payable to?

The Witness: The Atlantic & Pacific Bank & Trust Company.

The Court: All right, that nails it down.

Next question.

Q. Did you draw such a check? A. Yes, I did. A check was drawn.

The Court: Yes, I did.

Next question.

Q. What was the date of the check? A. It was either April 11 or 12, because it was picked up on the 12th.

Q. Picked up by whom? A. By a messenger from Rittmaster, Lawrence's office.

Q. Then what happened to the check? A. On Friday, the 13th, between 12:00 and 1:00 o'clock I received a call from an employee of The National Bank of North America requesting authority to certify that $100,000 check. I questioned the gentleman as to who was requesting certification and he said a Mr. Mori Schweitzer. I asked him to please put Mr. Schweitzer on the phone and I told Mr. Schweitzer that I felt that [51] this was not a usual procedure. He said, "Well, the only thing that will do for you," he said, "is if we certify it now your interest payments will start from today. Other than that I can't get it back to the bank until some time next week."

Q. By getting it back to the bank, what did he mean by that? What did you understand him to mean? A. To bring the check or mail the check to the Atlantic & Pacific Bank in the Bahamas.

Q. So that Aid Autc would lose interest until it was actually received by the Atlantic & Pacific Bank in the Bahamas, is that correct? A. This is what Mr. Schweitzer told me.

Q. Then what happened? A. It was during the lunch hour and my treasurer was out of the office and I didn't know the status of our funds on that day, so I told the gentleman at the bank he would have to wait until one o'clock until my treasurer came back. When Mr. Clayman, my treasurer, arrived back from lunch we checked and we found that based on the original stop order we had issued some checks to our suppliers against the $100,000 and, therefore, were not in a position to meet the second $100,000, though we would be within a few days.

is being entered, does not in any way show that consulting agreement creates exclusive agency duties by Rittmaster, Lawrence to or for or on behalf of Aid Auto Stores and in fact Mr. Klein conceded that there were no exclusive duties.

So it wasn't a kind of a situation where in what Mr. Lee has called a commercial bribery case, and which I take serious umbrage to in applying to this case. It wasn't a situation where we are dealing directly with someone we know to be a purchasing agent of Sears-Roebuck & Company [196] with exclusive and single duties to Sears-Roebuck & Company and we offer him a direct amount of money in order that he will purchase from us because there the kind of intent and knowledge is clearly shown upon the record.

There is no reason to believe that Sears-Roebuck's agent has any interest other than Sears-Roebuck. In this case there is all of the commercial business setting and reason in the world to believe that Arthur Rittmaster, being a financial consultant, and being an investor and being the head of a brokerage house, should be interested in possible deposits in banks in international investment.

So in this case we don't have any reason to presume knowledge of any relationship back to Aid Auto Stores by Mr. Cannon, and in fact there is none.

The only way that could be supplied is if as a matter of law the fact that this prospectus shows that it involved the Cannon, Jerold Company as a subunderwriter of a very small percentage of the shares—the knowledge of that prospectus can be

imputed to Mr. Cannon, and it can be held that mere knowledge of—the fact that the financial consultant relationship exists would preclude Mr. Cannon from dealing in any way with Mr. Rittmaster, as he has been proven to have dealt in this particular case, to have discussed the matter of loans from a bank in which he says [197] that he was interested, the Atlantic-Pacific Bank. I would suggest to the Court that as a matter of law that prospectus does not have the strength to prove those facts even if it could be imputed to Mr. Cannon and as a matter of law further it cannot be imputed to Mr. Cannon. The plaintiff would have to prove that Mr. Cannon had that knowledge or read the prospectus.

They have not forged that link.

Furthermore, your Honor, having not forged that link, but let's assume that they did for purposes of my further argument because as I say I would contend that you can't intend to induce someone to breach a relationship you don't know exists, but assuming that there is evidence from which a reasonable mind could conclude that Mr. Cannon did have knowledge of the relationship, and I dispute that, but assuming that, there must also be evidence in a case of serious import such as this, where we are in effect charging Mr. Cannon with crime.

The words "commercial bribery" constitute a violation of the penal law of the State of New York and involve also violations of numerous Federal statutes.

When we get to that point, and start pointing the finger of inducement such as this and when we

invade the financial world which lives and thrives on business [198] dealings, between investors, we must be circumspect in proving the issue of intent.

Now, what is evidence bearing upon Mr. Cannon's intent?

The Court: There I interfere long enough to tell you we will continue promptly at two o'clock, gentlemen, and we may have to keep the jury waiting, well, that is just too bad. I don't want to do it purposely. You have plenty of things to do and I know I have.

Very well, two o'clock promptly.

(Luncheon recess.)

[199] AFTERNOON SESSION

2:00 P.M.

(In open court; jury present.)

The Court: Won't you please proceed, Mr. Youtt.

Mr. Youtt: Thank you, your Honor.

Your Honor, when we recessed for lunch I had reached the next element of the Seventh claim, that being the element of intent and I was about to discuss that.

The question of intent, your Honor, could become a question for a jury if there were evidence from which reasonable minds could say, putting one fact together with another with whatever facts are available, that the plaintiff has carried the burden of proof, that Mr. Cannon intended to do what they claim he did. However, I would contend that those facts don't exist. As akin to the situation, the type

of facts exist are capable—in fact tend to support a theory of innocence far more than they support a theory of guilt based upon what has been charged in this case.

If we look at the evidence of intent I believe that the important evidence involving Mr. Cannon's contact with Rittmaster and Rittmaster & Lawrence in this case appear at Pages 88 to 91 of the deposition which is in evidence as it was introduced by the reading of it at the earlier stage of the presentation of the evidence. In [200] that passage the only thing that is established is that Mr. Cannon received two checks for $25,000 and that he had previously talked about those checks with Mr. Rittmaster and with Mr. Lawrence and with Mr. Schweitzer prior to the time that the Bahamas Bank certificate of deposit was issued.

There is nothing even linking the issuance of those loans to the deposit of the money in the testimony that has been presented as the plaintiff's case in chief and this is all that there is. This is what we must look at in determining whether or not there is evidence from which the inference of intent can be drawn.

Not even that link is there and there certainly isn't anything further to show that in some way Mr. Cannon conspired with Mr. Rittmaster to somehow defraud or to somehow force Mr. —cause Mr. Rittmaster to violate his fiduciary duties. Because of those facts, your Honor, and because in a case such as this so much depends upon that very element, this is a case that should not go to the jury.

Mr. Cannon should not be placed in a position where establishing the proposition that when you

deal with the director of a public corporation you deal with him at your peril and you cannot presume that he is going to act [201] honorably and honestly in connection with his dealings as a member of a board of numerous corporations. The fact is that Mr. Rittmaster was an investor, he was the head of a brokerage house. That is the way the initial contact was made. It was made from Mr. Rittmaster's firm to Mr. Cannon's firm. They talked about numerous things on their numerous meetings during the early months of 1973 and only in passing or only on a couple of occasions based upon this evidence did they talk about the Bahamas bank.

There was no theory that Mr. Cannon was dealing specifically with Mr. Rittmaster as an agent or fiduciary of Aid Auto Stores. He was dealing with him as a fellow man in the financial business and with that he had the right to deal with him—assuming that the facts are as they have been stated here, to just speak with him about these matters and as the facts are stated here, to deliver to him checks from a bank with whom he had contact before.

The Court: You said as stated here while you were waving the deposition. You mean as stated in the deposition?

Mr. Youtt: That is correct.

This basically is what I have to say with respect to the Seventh claim in the complaint.

There are, as your Honor will note, I think four [202] or five other—four other claims upon which the plaintiff seeks recovery against the defendants Cannon and Cannon, Jerold, three of them relating to the Securities Laws and one of them relating to

common law fraud. I am prepared to go through each one and argue each one should be dismissed.

With respect, your Honor, to the first claim, the first claim alleges the selling of an unregistered security and the engagement or the activity of Mr. Cannon in that process in violation of Section 12(1) of the Securities Law.

I would contend, your Honor, that certainly the plaintiffs have not focused or emphasized in any way at any time during the presentation of evidence the Securities Laws issue and they are seriously in default in establishing even a bare prima facie case on the first claim.

There is no evidence at all that the certificate of deposit was not registered. Nobody brought in evidence that this was not a registered security. So there can be no evidence from which a jury can conclude that Mr. Cannon engaged in the sale of an unregistered security.

Furthermore there is no evidence, there is no suggestion, there is no indication that this was part of a public offering. It is one certificate of deposit [203] in the United States.

I think if we went further into the evidence we would see it was virtually the only one, but the fact is that there is nothing to suggest that this was a public issue that required registration under the Securities Laws.

So for those reasons the first claim of the complaint should be dismissed. There is just not any evidence to support referral of to a jury for a determination of fact question.

And also there is a requirement under 12(1) commonly known as the privity requirement which

we addressed in our trial brief which requires that the person, in order to be liable under 12(1) be a person who sold. There is no evidence in this case to establish that Mr. Cannon was a person who sold the certificate of deposit in question.

The only evidence is that Mr. Cannon at some point discussed loans with Messrs. Rittmaster and Lawrence and Mr. Cannon testified in that deposition that he didn't even know when this particular certificate of deposit was sold until some later time.

So there is nothing linking Mr. Cannon in accordance with the privity requirement as being a person who sold the certificate of deposit to Aid Auto Stores and certainly significant there is the fact that Mr. Klein, [204] the president of Aid Auto Stores, has never heard of Mr. Cannon and he certainly never had any contact with him.

Finally in connection with this the plaintiff has argued in its trial memorandum that it has really gone on the theory that Mr. Cannon was a controlling person of the person who sold, and I am specifically referring to Page 12 of the trial memorandum of plaintiffs. They are claiming that Mr. Cannon should be liable because he was controlling Messrs. Rittmaster and Lawrence in this case.

Well, I suggest to your Honor that if there is evidence to show that Mr. Cannon caused Mr. Rittmaster and Mr. Lawrence to place this security or this certificate of deposit, that is some evidence of control, but it is not nearly the kind of evidence that is necessary to show that Mr. Cannon was in control, able to dictate and direct the powers and activities of Messrs. Rittmaster and Lawrence, so he

has not, on the facts on this record, established a control person. There are no facts to establish him to be a control person and certainly there aren't facts sufficient to send to a jury from which reasonable minds could conclude that he is a control person or was at the time. All of these go to the issue of the first claim in the complaint.

Going to the second claim of the complaint, [205] again the same claim is made to show that the plaintiff failed to show the privity connection, that the defendant was a person who sold and that's a defense which I raise equally in the second claim as I did in the first claim.

Since there is no such evidence this should not go to the jury.

Furthermore, in the second claim the question of 12(2), 12(2) involves the failure to provide information, the omission to state a material fact or the misstatement of a material fact to a person who ultimately purchases securities which causes that person to suffer a loss.

In this case the evidence I must say is again very cloudy as to what, if anything, there was of an omission. Mr. Klein testified that he received in May a copy of a financial statement, a statement which on its face showed that the bank had assets of some $3 million and it had the typical kind of bank liabilities and the one thing that was called to his attention that was particularly significant was the fact that as of the date of that financial statement, there were deposits of original depositors in a predecessor bank that hadn't yet been transferred. That was the day after the bank took over from its predecessor.

There is no evidence at all that that statement [206] reflected the condition of the Bahamas Bank at the time that the certificate of deposit was purchased. For all we know from the evidence in this case all of those transfers had been successfully made and as Mr. Klein testified, that would remove a lot of his objections to the condition of the bank.

They did not go one step to establish what the condition of the bank was. It was their obligation, if they are going to allege that there was a misstatement or an omission, to establish that the condition of the bank on April 3 or 13 was in such a condition as to be—as to involve a misstatement of the facts which were available to Mr. Klein. They didn't do that. They didn't show anyt-ing as to the condition of the bank at that time. They didn't make an effort to before this Court. So, therefore, this Court does not have anything from which to judge what in fact a misstatement of fact could involve. This Court has a November 1st financial statement and this Court cannot conclude from that that reflected the condition on April 3 or May 25 or April 13 or any other date than November 1st, and at November 1st I would suggest to this Court that there is nothing unusual about the fact that certain deposits had not yet been transferred from a bank that had just previously left—had previously transferred [207] its assets on the day before.

For these reasons, your Honor, I would argue that there was no omission. There is no evidence in the record from which a jury can reasonably find an omission or a misstatement, either on the part of Mr. Rittmaster or on the part of Mr. Cannon.

Certainly on the part of Mr. Cannon because he made no statements whatsoever that have been proven as a matter of record in this case.

Also, your Honor, again there is a matter of defense. It is established that if the plaintiff, or if the person who loses on a transaction knew the true facts, notwithstanding the omission, notwithstanding the misstatement, if somehow he had independent knowledge or strong access to that knowledge, he doesn't recover under 12(2).

The evidence in this case shows that the plaintiff had access to Mr. Rittmaster, who should have been doing his job, who should have investigated the bank, who should have gotten a standard financial statement as of the condition of that bank at the time of the placement of this certificate of deposit.

The evidence also shows that Mr. Rittmaster himself was in contact with officers of the bank and the evidence further shows that Mr. Klein himself was also [208] in contact with the president of the bank on the date that the money was paid. That certainly proves that the plaintiff had ample access to the type of information which if the bank was in a different condition than they assumed it was could have informed them, provided them with the necessary information. Because they had that access and because that that as a matter of record shows right now and because there is nothing further which supports their claim of liability against Mr. Cannon, again on the second claim of the complaint, that is another reason why it, too, should be dismissed.

Further, another reason is that there is a question of whether or not this was a material misstatement or material omission.

The fact is Mr. Klein has testified that he relied not on Mr. Rittmaster, not on what plaintiffs must assume is the source of Mr. Cannon's involvement in this case, Mr. Rittmaster, but rather on his counsel, Mr. Beigen.

In order to make the decision to invest in the Bahama Bank he waited for several days until he got the go-ahead from Mr. Beigen. Mr. Beigen hasn't testified here. Mr. Beigen hasn't shown us that he got information from Mr. Cannon, which he did not.

Mr. Beigen hasn't shown us what kind of a [209] search he did. But we do have evidence that Mr. Beigen came back and said go ahead. If anybody was the person upon whom Mr. Klein relied in this case, it was Mr. Beigen and it was not Mr. Rittmaster or through Mr. Rittmaster or anything Mr. Cannon may or may not have said, which is not a part of the record in this case.

Going on now to the third claim. The third claim is a claim under Section 10(b) of the Securities and Exchange laws of 1934.

Again in this case, as we have outlined in our trial memorandum, there are numerous elements that must be proved. Again in this case there is no proof in terms of actual fraud, in terms of actual wrongdoing. There is no proof of the true condition of the bank at the time in question, at the time the certificate of deposit was purchased.

For all we know from this record that bank could have been in an immaculate condition at that time. It could have been going strong. It could have been very positive. There is no proof from which we can say Mr. Cannon or anybody else made a misstate-

ment of fact to Mr. Klein or to Aid Auto Stores, or to anybody else.

Because of that we can't even conclude the threshold question that the purchase was made on the basis [210] of an omission or material misstatement of any kind of fraud.

Further, going down the list on that, there was no reliance which must be established as an element under 10(b)5. There is no reliance by Mr. Klein or Aid Auto Stores upon anything that Mr. Rittmaster said about the condition of the bank.

In fact, again Mr. Klein states he relied upon the advice of his counsel, Mr. Beigen. Mr. Beigen hasn't been tied to Mr. Cannon or anything that Mr. Cannon did or said or did not do at all. This was the reliance upon which Mr. Klein focused.

Furthermore, there was nothing that Mr. Klein—the fact that Mr. Klein entered into this investment, really didn't involve the condition of the bank. He assumed that the bank was in good condition, but he wasn't shopping for the bank that was in the best condition. He didn't ask any questions about the New Jersey bank that Mr. Rittmaster suggested. He didn't ask any questions about this. He went into it for the public relation purpose of expanding friendly relations with other banks so that he could utilize them in the future when he was in the process of getting into other acquisitions.

So again we don't have reliance upon anything [211] of a misstatement, whatever that misstatement may have been, and I contend that nothing in the nature of a misstatement has been established in this case.

So we don't have reliance, we don't have any proof of insolvency or virtual insolvency, such as the plaintiffs have alleged in their complaint, and furthermore we don't have the important element of scienter, the element of intent to defraud, the element of intent by Mr. Cannon to do something wrong.

That question, the question of scienter again merge to a large extent with the question I have argued in connection with the Seventh claim of the complaint, that being the question of intent as it bears upon procuring the breach of duty of a fiduciary officer.

If there is evidence under the Seventh claim, then certainly that evidence could be evidence of scienter, but I contend that that evidence doesn't exist equally for the Seventh claim purpose or for purposes of the Third claim of the complaint.

We now get to the fourth claim of the complaint which is common law fraud and again basically the common law fraud elements have not been established. I am not going to spend a lot of time on this because it goes over the area I have been on in 10(b)5 and the Seventh claim [212] of the complaint. I have gone over each of these to show that with the exception of the Seventh claim of the complaint the plaintiff didn't make any effort to present evidence about this.

Mr. Lee argued to the jury in his opening statement that the whole theory was commercial bribery and he conducted this case only to show that and I contend that that too is insufficient, that should be dismissed, but in the Securities Law case, the common law fraud case has been treated as if it has been virtually abandoned and it hasn't formally

been abandoned and that is why I am spending time on it.

Now, a couple of more areas. Because Mr. Lee didn't make an effort to prove his Securities Law case, because from the opening of this case, from his trial law memorandum and from his statements to the Court and jury, he showed he was only focusing upon what he calls the commercial bribery case.

I think this Court should take notice of the fact that the only reason we are before this Court in this Federal jurisdiction is because of the Securities Law issue and under my understanding of jurisdiction, if a Federal cause of action is honestly and sincerely promoted and put forward as a theory of the case, that establishes the [213] jurisdiction.

I would contend that that hasn't been established in this case, that no effort has been made to establish the source of Federal jurisdiction, leaving us only with the State law claim. If we look at the State law claim, and I think Mr. Lee anticipated this in his trial memorandum on the first page where he says that this case is based not only upon the Federal statute but upon diversity of citizenship. He was thinking of the possibility that we would have to go on a separate jurisdictional basis. Diversity of citizenship does not exist in this case.

So far as the record shows, the principal place of business of Aid Auto Stores, Inc., is New York. The principal place of business of Cannon, Jerold & Company is also New York, and there must be as an axiom of jurisdiction complete diversity between all parties. The fact that that diversity doesn't exist means that we must rely upon the Federal

claim and pendent jurisdiction and I would ask this Court, among other reasons, to dismiss this case because it is not here on a proper jurisdictional basis.

Finally, your Honor, there has been no proof at all of the fact that the Bahamas Bank is out of business, if in fact it is. There has been no proof that Mr. Klein's company, Aid Auto Stores, has really suffered this loss.

[214] For all we know, based upon the record in this case, the bank could be there or it could be in liquidation or it could have sufficient, ample assets to pay Mr. Klein dollar for dollar everything that he lost. I am saying that as a technical matter. That evidence has not been established and reasonable minds cannot conclude that there were any damages or any loss suffered in this case in connection with the total loss of the certificate of deposit.

They would have to speculate. Under the law they shouldn't have to speculate and reasonable minds cannot differ on that issue, so that is an additional reason why this case should be dismissed.

For all of the reasons I have enumerated in this argument, I would ask that this Court grant the motion under Rule 50A and direct a verdict in favor of the defendants Cannon and Cannon, Jerold, and accordingly appropriately enter a judgment.

The Court: Mr. Lee.

Mr. Lee: Thank you, your Honor. May it please the Court, addressing myself first to the 10B claim, the Federal fraud, the Court has not had the opportunity to look at the exhibits introduced before the jury this morning, including evidence which showed

that Mr. Cannon bought the [215] cow with her own milk. He took $100,000 out of the Bahamian bank for his own personal benefit whereas he had made available to a stockholder upstream the moneys which apparently midwifed the acquisition of his corporate shell from a Calgary bank. That is in the evidence which was submitted this morning to the jury and is in evidence.

The Court: Just a moment, gentlemen. Mr. Lee remained absolutely silent while argument was advanced by Mr. Youtt and I want him now to get the same consideration at your hands.

Please do not talk.

Go ahead, Mr. Lee.

Mr. Lee: In addition, in connection with Mr. Cannon's trip to Nassau, the Bahamas, shortly prior to the date of the certificate of deposit, he bared his own notes consisting of three pages describing the assets of the corporation and that is Exhibit 10 in evidence.

At the time of the transaction, the sale of the certificate of deposit, it is quite clear from what is already in evidence and which the jury can weigh under Section 10(B), it is quite clear that what we are dealing with is in effect a Ponzi-type of scheme, the use of a corporate shell and the use of an effort to make money available in the first place to buy the stock of this shell [216] and get either the same charter modified or a new charter, the record is quite uncertain on that, and then once the money is put up take it out of the bank on the bottom and that is why we introduced that evidence.

So I think that is certainly sufficient for Section 10(B) to go to the jury.

Now, in connection with diversity of citizenship, Aid Auto Stores is a Delaware corporation. Mr. Cannon is a New Jersey resident. Certainly we are here as well on diversity.

Returning to what I think Mr. Youtt properly states is what we feel to be the simple thrust of this case, I think he omits entirely the fact that his client has the burden of proof to show that there was full disclosure to the board of directors. Not because Mr. Cannon was a member of the board of directors, but rather he was knowingly dealing with a fiduciary. He is absolutely charged with the knowledge that appears in that prospectus in which he was the third largest underwriter, namely that Rittmaster, Lawrence & Company was an agent, that Rittmaster, Lawrence & Company was going to designate, although no director had been designated—was going to designate a director on the board.

It is clear on the record that that director [217] was designated.

Now, Mr. Rittmaster and Mr. Cannon had a number of meetings, which were read into the record. Without further testimony from Mr. Cannon, the jury is entitled to look at those conferences, look at the fact that he is charged with the knowledge that appears on the face of it and see that he has actual knowledge—actual knowledge of the fiduciary relationship between Rittmaster and the corporation and then it is entirely up to Mr. Cannon to carry his burden of showing full disclosure and as we repeated the famous words, in all its stark significance.

We simply don't have the problem of proving intent in that aspect of it. He has the absolute duty of showing the full disclosure to the board of directors.

What did Mr. Cannon himself do as the record is clear? He personally physically delivered the checks through his office to Mr. Rittmaster and Mr. Lawrence for $25,000 unsecured loans. These members of the jury are entitled to know whether an unsecured loan, which takes place simultaneously or substantially simultaneously with the corporate C.D. —they are entitled to weigh that. They are entitled to know how that was disclosed and indeed Mr. Cannon must attempt to disclose it.

That I think, your Honor, is a sufficient outline [218] of what is presently in the record which must go to the jury.

The Court: Will you be good enough, Mr. Clerk, to gather the exhibits produced into evidence. The Court will take a short recess and reserve decision and we hope to be back in 15 or 20 minutes and announce our determination.

(Recess.) (Jury absent.)

The Court: The criterion for the resolution of the pending motion for a directed verdict is found in Diapulse Corporation against Birtcher Corporation, 362 Fed. 2d 736 at Page 743, Second Circuit, 1966.

"The directed verdict device was designed to be utilized in appropriate cases to spare the jury from a lengthy deliberation when the evidence did not warrant it. When a party moves for a directed verdict, the trial Judge must determine as a matter of law whether there is sufficient evidence to take the

case to the jury. Only if reasonable men could not reach differing conclusions on the issue may the question be taken from the jury."

Baker against Texas & Pacific Railroad Company, 359 U.S. 227, 228, 1959.

We are constrained to do and find as a matter of law that the totality of proof adduced at trial up to [219] this point falls far short of sustaining the elements which the law makes imperative as to each of the separate claims asserted herein.

We say without reservation that there is no evidence to either support or sustain the claim of scienter, fraud, misrepresentation, commercial bribery or even the Ponzi game to which Mr. Lee made reference. Even the proof that was addressed to portions of the claims asserted was in the main very thin indeed, and forces the fact finder to pile inference upon inference.

We endorse in general the points advanced in argument by counsel for defense on this motion. It obviates the necessity on our part of further delineation in support of our determination to grant the motion.

Accordingly, we declare as a matter of law that the evidence adduced is insufficient to take the case to the jury. We grant the motion for a directed verdict. We dismiss the complaint in its entirety as between the litigants before us and direct that judgment be entered in favor of the defendants against the plaintiff. We shall now discharge the jury from further participation in this case.

Mr. Youtt: Thank you, your Honor.

The Court: Send for the jury.

Motion to Dismiss

[220] (Jury present.)

The Court: Ladies and gentlemen of the jury, we regret to have kept you waiting, but there were very important questions of law that were argued at length by counsel. We have just decided and declared on the record that as a matter of law there is insufficient evidence to warrant that this case be turned over to you for resolution with respect to any aspect of the claims asserted. Accordingly with the thanks of counsel and the Judge you are discharged from further participation in the case.

It is now 3:40. Thank you, ladies and gentlemen, for your part up to this moment.

(Jury excused.)

The Court: Gentlemen, if you will be good enough to forebear with the Court, we would like to have the record show that the correct citation for the Diapulse Corporation case is not 262, but it is 362 Fed. 2d.

Mr. Clerk, will you be good enough to announce an adjournment until tomorrow morning at ten o'clock.

The Clerk: Court stands adjourned until tomorrow morning at 10:00 o'clock. All rise, please.

(Adjourned.)

Memorandum Opinion by Irving Ben Cooper, *D.J.*

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

Defendants Cannon and Cannon Jerold, Inc. move to assess as taxable costs against the plaintiff corporation the reasonable expenses consisting only of attorneys' fees incurred in connection with the defense of this action. The motion, made pursuant to Section 11(e) of the Securities Act of 1933, 15 U.S.C. §77k(e), requests the total sum of $8,480.

Section 11(e) of the Securities Act of 1933 provides that costs may be assessed against a losing party if the Court believes the suit to be "without merit." This standard has been interpreted to mean that before awarding counsel fees the Court must find that the claim borders on frivolity or is brought in bad faith. *Klein* v. *Shields & Co.*, 470 F. 2d 1344, 1347 (2d Cir. 1972); *Colonial Realty Corp.* v. *Brunswick Corp.*, 337 F.Supp. 546, 553 (S.D.N.Y. 1971); *Katz* v. *Dalka Research Corp., modified, sub nom., Katz* v. *Amos Treat & Co.*, 411 F.2d 1046 (2d Cir. 1969).

There is no doubt that the claims under the securities laws asserted here border on frivolity. There was no proof that the certificate of deposit was part of a public offering or that it was unregistered, or that defendants were persons who sold within the meaning of the Securities Act of 1933, as required under Sections 12(1) and 12(2) of that Act. 15 U.S.C. §§77*l*(1); 77*l*(2). (Complaint, Claims 1, 2).

Memorandum Opinion by Irving Ben Cooper, D.J.

Moreover, no proof was adduced that defendants made material misstatements or omissions, or that defendants possessed the necessary scienter, or that plaintiff to his detriment relied thereon. Lacking these crucial elements in its claim under Section 10(b), 15 U.S.C. §78j(b) (Complaint, claim 3), and common law claim (Complaint, claim 4), plaintiff's suit bordered on frivolity.

Further, the Court finds that the pendent claim against defendants of inducing a breach of loyalty on the part of one of plaintiff's directors (Complaint, claim 7) was instituted in bad faith. The principal thrust of the seventh claim was that defendant Cannon had committed "commercial bribery." This serious charge—made first in plaintiff's opening (Tr. 3, 10),[1] repeated in its oral argument against defendants' motion for a directed verdict (Tr. 215-16), and in opposition to the present motion (Pl. Aff. in Opp. at paras. 7, 8)—was totally unsupported at trial. No evidence was adduced that defendant Cannon had knowledge that Mr. Rittmaster had an exclusive relationship with plaintiff corporation,[2] or that Cannon sought to mislead Rittmaster. In fact Rittmaster's dealings with the Bahamas bank were totally consonant with legitimate business practices, as plaintiff's president conceded. (Tr. 141-43). In short, the totality of the evidence advanced fell woefully short of a prima facie claim on this charge as well as on the claims under the securities laws.

The inherent weakness and inadequate nature of the total proof available to plaintiff should have been overwhelmingly apparent not only at trial time but long before that. Plaintiff should have known that it proceeded at

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[1] References are to the trial transcript.

[2] Indeed, Rittmaster had a non-exclusive arrangement with the plaintiff corporation. (Tr. 144-45; 148-49).

its peril. Plaintiff's deportment here was reckless indeed, to say the very least.

This plaintiff and others to come should be discouraged from hurling unfounded and specious allegations where irreparable damage to the reputations of others may ensue. See *Stratton Group* v. *Chelsea Nat. Bank,* 54 F.R.D. 227, 228 (S.D.N.Y. 1972).

Accordingly, in addition to costs to be awarded the defendants, the judgment to be entered herein will provide for attorneys' fees in the amount of $8,480, the reasonableness of which is not contested, the plaintiff's contention being solely that the Court is without power in these circumstances to make any award for counsel fees.

So Ordered:

New York, N.Y.
January 27, 1975

Irving Ben Cooper
United States District Judge

Judgment

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

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73 Civ. 4890

This action having come on for trial on November 19, 1974 by plaintiff against defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc. before the Court and a jury, Hon. Irving Ben Cooper, District Judge, presiding, and the Court on motion of defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc. having directed a verdict for said defendants; and

It appearing that the cross-claim of defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc. against defendants Mori Aaron Schweitzer, David A. Wooldridge, Arthur Rittmaster, Jr., Lee Lawrence and Emanuel Iwanier has thereby been rendered moot; and

It further appearing that plaintiff and defendants Arthur Rittmaster, Jr., Lee Lawrence and Rittmaster, Lawrence & Co., Inc. have by separate agreement consented to the entry of judgment against defendants Arthur Rittmaster, Jr. and Lee Lawrence and to the dismissal of third party defendants Murray Klein, Herbert Eisenberg, Arnold Biegen, Milton Wallace, Luis Neufeld, Seymour Cohen, Martin Goldberg, Morris Clayman and Irving Poploff; and

The plaintiff having consented to dismissal of this action against all other defendants who were served but did not appear at the trial;

Judgment

IT IS ORDERED, ADJUDGED AND DECREED that the complaint herein be and the same is hereby dismissed against defendants Herbert S. Cannon, Cannon, Jerold & Co., Inc. and all other defendants appearing herein, that the cross-claim of defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc. be dismissed as moot, and that the third party complaint be dismissed.

Dated: New York, New York
December 12, 1974

IRVING BEN COOPER
U.S.D.J.

JUDGMENT ENTERED—12-13-74
/s/ RAYMOND F. BURGHART

Notice of Appeal

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE]

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73 Civil 4890

SIRS:

NOTICE is hereby given that plaintiff Aid Auto Stores, Inc. hereby appeals to the United States Court of Appeals for the Second Circuit from so much of a judgment entered on December 13, 1974 against plaintiff as dismissed this action on the merits in favor of defendants Herbert S. Cannon and Cannon, Jerold & Co., Inc.

Dated: New York, New York
December 20, 1974

Yours, etc.

ROGERS HOGE & HILLS
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Notice of Appeal

To:

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